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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

**FORM 6-K**

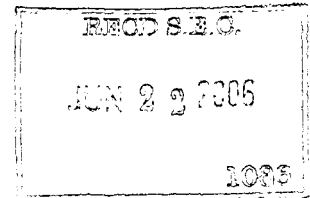
**Report of Foreign Private Issuer Pursuant to Rule 13a-16 or 15d-16  
Under the Securities Exchange Act of 1934**

Date of Report June 20, 2006

Commission File No. 0-29004

**NOVATEL INC.**

1120 - 68<sup>th</sup> Avenue N.E., Calgary, Alberta, Canada T2E 8S5  
(Address of Principal Executive Office)



P.E.  
6-2006

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F.      Form 20-F ☒      Form 40-F ☐

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1):    Yes ☒    No ☐

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7):    Yes ☐    No ☒

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.    Yes ☐    No ☒

If "Yes" is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-N/A.

PROCESSED

JUN 30 2006  
THOMSON  
FINANCIAL

A copy of the Registrant's Annual Report to Shareholders for the fiscal year ended December 31, 2005 is furnished herewith but is not incorporated by reference into any other documents.

### **EXHIBITS**

The following information is furnished to the SEC.

<u>No.</u>	<u>Document</u>
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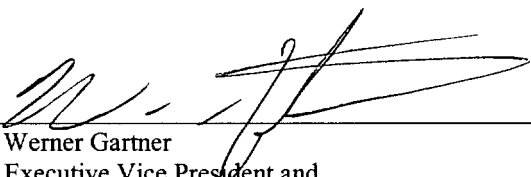
- |     |  |
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| (1) | Annual Report to Shareholders for the fiscal year ended December 31, 2005. |
|-----|--|

### **SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

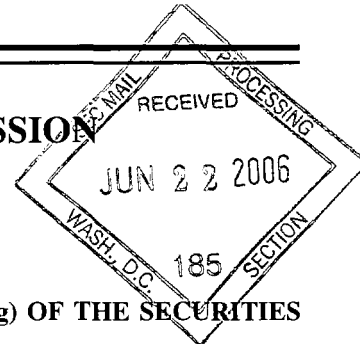
NOVATEL INC.

Date: June 20, 2006

  
\_\_\_\_\_  
Name: Werner Gartner  
Title: Executive Vice President and  
Chief Financial Officer

## EXHIBIT 1

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549  
**FORM 20-F/A**  
(Amendment No. 1)



☐ **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934**

**OR**

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2005

**OR**

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission file number 0-29004

**NOVATEL INC.**

(Exact name of Registrant as specified in its charter)

N/A

(Translation of Registrant's name into English)

Canada

(Jurisdiction of incorporation or organization)

1120-68<sup>th</sup> Avenue N.E., Calgary, Alberta, Canada T2E 8S5

(Address of principal executive offices)

SECURITIES REGISTERED OR TO BE REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT: **NONE**

SECURITIES REGISTERED OR TO BE REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

**Common Shares**

(Title of Class)

SECURITIES FOR WHICH THERE IS A REPORTING OBLIGATION PURSUANT TO  
SECTION 15(d) OF THE ACT: **NONE**

At December 31, 2005, Registrant had outstanding 8,365,150 Common Shares, no par value.

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes ☐

No ☒

If this report is an annual or transition report, indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act 1934.

Yes ☐

No ☒

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports) and (2) has been subject to such filing requirement for the past 90 days.

Yes ☒

No ☐

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☐

Accelerated filer ☒

Non-accelerated filer ☐

Indicate by check mark which financial statement item the Registrant has elected to follow.

Item 17 ☐

Item 18 ☒

If this is an annual report, indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ☐

No ☒

## EXPLANATORY NOTE

*This Amendment No. 1 to Form 20-F is being filed solely to include the conformed signature pages to the Form 20-F and Exhibits 31.1, 31.2, 32.1 and 32.2, which were inadvertently omitted from the original filing, and an updated Exhibit 23.1.*

\*\*\*

*The dollar amounts presented in this Annual Report on Form 20-F are in Canadian currency unless otherwise noted (CDN\$1 = U.S. \$0.9037 on May 4, 2006), and are presented in accordance with accounting principles generally accepted in Canada. Historic rates of exchange appear in Part I, "Item 3 — Key Information, Selected Financial Data." The material differences between Canadian and U.S. generally accepted accounting principles ("GAAP") which would bear upon NovAtel Inc.'s, (hereinafter referred to as "NovAtel" or "the Company"), financial statements and, more particularly, income applicable to shareholders' equity are disclosed in Note 23 of Notes to Consolidated Financial Statements.*

*Certain statements in this Annual Report, including those about the Company's future plans and intentions, financial guidance, long-term growth prospects, levels of activity or other future events, are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are not based on historical facts but rather on management's current expectations regarding NovAtel's future growth, results of operations, performance, future capital and other expenditures, competitive advantages, business prospects and opportunities. Wherever possible, words such as "anticipate", "believe", "expect", "may", "could", "will", "potential", "intend", "estimate", "should", "plan", "predict", "forecast" or the negative or other variations of these words, or similar words or phrases, have been used to identify these forward-looking statements. Forward-looking statements involve significant known and unknown risks, uncertainties and assumptions. Many factors could cause actual results, performance or achievements to differ materially from the results discussed or implied in the forward-looking statements, including operating results of the Company's joint venture Point, Inc. ("Point"), impact and timing of large orders, U.S. dollar to Canadian dollar exchange rate fluctuations, establishing and maintaining effective distribution channels, certification and market acceptance of NovAtel's new products, impact and timing of large orders, credit risks of customers and the Company's joint venture Point, Inc. ("Point"), pricing pressures in the market and other competitive factors, maintaining technological leadership, timing of revenue recognition in connection with certain contracts, the ability to maintain supply of products from subcontract manufacturers, the procurement of components to build products, product defects, the impact of industry consolidations, vulnerability to general economic, market and business conditions, competition, environmental and other actions by governmental authorities, reliance on key personnel and other factors described in this Annual Report and other SEC filings, many of which are beyond the control of NovAtel. These factors should be considered carefully and undue reliance should not be placed on the forward-looking statements. These forward-looking statements are made as of the date of this Annual Report, and NovAtel assumes no obligation to update or revise them to reflect new events or circumstances.*

## **PART I**

### **Item 1. Identity of Directors, Senior Management and Advisers**

Not applicable.

### **Item 2. Offer Statistics and Expected Timetable**

Not applicable.

### **Item 3. Key Information**

#### **A. Selected Financial Data**

##### **(a) Summary Financial Information**

The following table sets forth selected financial data of the Company for the periods indicated. The selected financial data as at December 31, 2004 and 2005 and for the years ended December 31, 2003, 2004 and 2005 have been derived from our audited consolidated financial statements, which appear elsewhere in this Annual Report. The selected financial data as at and for the years ended December 31, 2001 and 2002 and as at December 31, 2003 have been derived from our audited consolidated financial statements, not included in this Annual Report. The table sets forth, in Canadian dollars and U.S. dollars, the selected financial data as prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). The financial data should be read in conjunction with "Item 5 — Operating and Financial Review and Prospects" and the Consolidated Financial Statements of the Company and Notes thereto included elsewhere in this Annual Report.

	Year Ended December 31				
	2005	2004	2003	2002	2001
	(in thousands, except per share data)				
<b>Statement of Operations Data (1)</b>					
Revenues:					
Product sales .....	\$59,306	\$48,802	\$32,138	\$26,967	\$23,241
NRE fees .....	3,989	5,130	6,546	6,179	4,996
Total revenues .....	<u>63,295</u>	<u>53,932</u>	<u>38,684</u>	<u>33,146</u>	<u>28,237</u>
Cost of sales:					
Cost of product sales .....	22,323	19,586	14,805	11,885	10,730
Cost of NRE fees .....	2,313	2,917	3,565	4,055	2,542
Total cost of sales .....	<u>24,636</u>	<u>22,503</u>	<u>18,370</u>	<u>15,940</u>	<u>13,272</u>
Gross profit .....	38,659	31,429	20,314	17,206	14,965
Operating expenses:					
Research and development .....	10,882	9,588	7,123	5,334	6,571
Selling and marketing .....	6,387	5,751	5,269	5,361	3,612
General and administration .....	7,082	5,312	4,280	4,045	3,711
Foreign exchange (gain)loss .....	255	595	527	(49)	(5)
Share offering costs .....	—	754	—	—	—
Total operating expenses .....	<u>24,606</u>	<u>22,000</u>	<u>17,199</u>	<u>14,691</u>	<u>13,889</u>
Operating income .....	14,053	9,429	3,115	2,515	1,076
Interest income, net .....	787	313	174	84	131
Other expense .....	(72)	(67)	(137)	(377)	(128)
Benefit of investment tax credits .....	1,592	4,356	—	—	—
Income from continuing operations before income taxes .....	16,360	14,031	3,152	2,222	1,079
Income taxes					
Current provision .....	2,046	2,328	52	77	13
Future income tax expense (benefit) .....	(2,402)	(1,091)	—	—	—
Total income tax expense (benefit) ...	<u>(356)</u>	<u>1,237</u>	<u>52</u>	<u>77</u>	<u>13</u>
Net income from continuing operations (3) .....	16,716	12,794	3,100	2,145	1,066
Income (loss) from discontinued operations (3) ...	—	21	360	(648)	(956)
Net income .....	<u>\$16,716</u>	<u>\$12,815</u>	<u>\$ 3,460</u>	<u>\$ 1,497</u>	<u>\$ 110</u>
Net income (loss) per share (basic):					
Continuing operations .....	\$ 2.01	\$ 1.59	\$ 0.40	\$ 0.28	\$ 0.14
Discontinued operations .....	—	—	0.05	(0.09)	(0.13)
Net income per share .....	<u>\$ 2.01</u>	<u>\$ 1.59</u>	<u>\$ 0.45</u>	<u>\$ 0.19</u>	<u>\$ 0.01</u>
Weighted average shares outstanding (basic) ...	<u>8,298</u>	<u>8,063</u>	<u>7,723</u>	<u>7,681</u>	<u>7,690</u>
Net income (loss) per share (diluted):					
Continuing operations .....	\$ 1.91	\$ 1.51	\$ 0.39	\$ 0.27	\$ 0.14
Discontinued operations .....	—	—	0.04	(0.08)	(0.13)
Net income per share .....	<u>\$ 1.91</u>	<u>\$ 1.51</u>	<u>\$ 0.43</u>	<u>\$ 0.19</u>	<u>\$ 0.01</u>
Weighted average shares outstanding (diluted) ....	<u>8,763</u>	<u>8,500</u>	<u>7,983</u>	<u>7,824</u>	<u>7,704</u>

Footnotes appear on pages 6-10

Year Ended  
December 31, 2005

(in thousands, except  
per share data)

**(U.S. \$ equivalent) (2)**

Revenues:	
Product sales .....	\$53,595
NRE fees .....	<u>3,605</u>
Total revenues .....	<u>57,200</u>
Cost of sales:	
Cost of product sales .....	20,173
Cost of NRE fees .....	<u>2,091</u>
Total cost of sales .....	<u>22,264</u>
Gross profit .....	34,936
Operating expenses:	
Research and development .....	9,834
Selling and marketing .....	5,772
General and administration .....	6,400
Foreign exchange loss .....	<u>230</u>
Total operating expenses .....	<u>22,236</u>
Operating income .....	12,700
Interest income, net .....	711
Other expense .....	(65)
Benefit of investment tax credits .....	<u>1,439</u>
Income from continuing operations before income taxes .....	14,785
Income taxes	
Current provision .....	1,850
Future income tax expense (benefit) .....	<u>(2,171)</u>
Total income tax expense (benefit) .....	<u>(321)</u>
Net income .....	<u>\$15,106</u>
Net income per share (basic):	
Continuing operations .....	\$ 1.82
Discontinued operations .....	<u>—</u>
Net income per share .....	<u>\$ 1.82</u>
Weighted average shares outstanding (basic) .....	<u>8,298</u>
Net income per share (diluted):	
Continuing operations .....	\$ 1.72
Discontinued operations .....	<u>—</u>
Net income per share .....	<u>\$ 1.72</u>
Weighted average shares outstanding (diluted) .....	<u>8,763</u>

Footnotes appear on pages 6-10



	December 31,					U.S. \$
	(Canadian \$)					Equivalent
	2005	2004	2003	2002	2001	December 31,
	(in thousands)					2005 <sup>(2)</sup>
<b>Balance Sheet Data<sup>(1):</sup></b>						
Working capital .....	\$44,270	\$30,322	\$17,978	\$14,372	\$12,284	\$40,007
Total assets .....	71,255	52,946	35,572	30,890	27,821	64,393
Long-term liabilities .....	—	—	212	98	253	—
Total shareholders' equity .....	58,117	40,093	25,447	20,547	19,086	52,520

- (1) The consolidated financial statements have been prepared in accordance with generally accepted accounting principles in Canada (Canadian GAAP or Canadian principles). The material differences from U.S. generally accepted accounting principles (U.S. GAAP or U.S. principles) are described below.
- (2) Canadian dollar amounts for 2005 have been translated into U.S. dollars solely for the convenience of the reader, at the rate of U.S. \$0.9037 per CDN \$1.00, which was the exchange rate as of May 4, 2006. These translations are not necessarily representative of the amounts that would have been reported if the Company historically had reported its financial statements in U.S. dollars. In addition, the rates utilized are not necessarily indicative of the rates in effect at any other time.
- (3) As of December 31, 2005, the Company owned a 70% equity interest in Mezure, Inc., a company that had been developing a GPS, wireless communication and Internet based product for deformation monitoring of manmade and natural structures. On April 8, 2003, the shareholders of Mezure voted unanimously to proceed with a Chapter 7 bankruptcy filing for Mezure, which was concluded on September 24, 2003. Consequently, the Company is treating Mezure as a discontinued operation.

#### Canadian GAAP to U.S. GAAP Reconciliation (\$ thousands)

##### i) *Deferred Development Costs*

As of December 31, 2005, the Company had deferred \$1,657 of development costs, net of accumulated amortization related to the development of a certified aviation GPS receiver. In the year ended December 31, 2005, the Company deferred \$nil of development costs (\$218 in 2004, \$157 in 2003, \$125 in 2002, and \$4 in 2001) in accordance with Canadian GAAP. Under U.S. GAAP, these costs would be expensed as incurred as research and development costs.

In the year ended December 31, 2005, the Company amortized \$538 of deferred development costs (\$416 in 2004, \$196 in 2003, \$57 in 2002, and \$36 in 2001) in accordance with Canadian GAAP. Under U.S. GAAP, these costs would have been expensed in the periods when the originating expenditures were incurred.

Further, for U.S. GAAP purposes, the Company would have recharacterized the goodwill acquired on the Mezure, Inc. share acquisition of \$231 as development related costs, and these costs would have been expensed on acquisition in 2001.

In addition, for Canadian GAAP purposes, in connection with the recognition of prior year's investment tax credits, the Company reduced the deferred development costs by \$164 in the year ended December 31, 2005. Under U.S. GAAP, this amount would have been accounted for as an expense when the originating expenditures were incurred.

##### ii) *Stock-Based Compensation*

Under U.S. GAAP, Statement of Financial Accounting Standard ("SFAS") 123 "Accounting for Stock-Based Compensation" establishes a fair value based method of accounting for stock-based compensation. Companies have the option of including the effect of this pronouncement in determining their net income, or alternatively, may

continue to apply the accounting provisions of APB Opinion 25, but must comply with the disclosure requirements of SFAS 123. For U.S. GAAP purposes, the Company continues to account for its stock-based compensation in accordance with APB Opinion 25 (see Note 23(k) in the consolidated financial statements presented elsewhere in this Annual Report).

Effective January 1, 2004, under Canadian GAAP the Company adopted the fair value method of accounting for stock options awarded to employees on or after January 1, 2002 as required by amended CICA Handbook Section 3870 *Stock-Based Compensation and Other Stock-Based Payments*. As permitted by the transitional provisions of Section 3870, the change was adopted retroactively without restatement. Under Section 3870, the fair value of stock options is recognized over the applicable vesting period as stock-based compensation expense and a credit to contributed surplus. When options are exercised, the proceeds are credited to share capital, and the applicable fair value is reclassified from contributed surplus to share capital. Retroactive application of Section 3870 resulted in the opening balances as at January 1, 2004 of deficit, contributed surplus and share capital being increased by \$456, \$390 and \$66, respectively, as though the fair value method had been applied since January 1, 2002. As indicated above, the Company continues to account for its stock-based compensation in accordance with APB 25 and thus these adjustments would not be recorded for U.S. GAAP purposes.

Under Canadian GAAP, the Company incurred stock-based compensation expense of \$587 in the year ended December 31, 2005 (\$326 in 2004). For U.S. GAAP purposes, this expense would not have been included in the determination of net income.

### **iii) *Derivatives and Hedging Activities***

The Company has historically entered into foreign exchange options and forward contracts to manage its exposure to foreign currency fluctuations. Under U.S. GAAP, the accounting for derivative instruments and hedging activities is contained in the Statement of Financial Accounting Standard ("SFAS") No. 133, as amended by SFAS 137, SFAS 138 and SFAS 149 ("SFAS 133"). SFAS 133 establishes accounting and reporting standards requiring that all derivative instruments be recorded in the balance sheet as either an asset or a liability measured at fair value and requires that changes in the fair value be recognized currently in earnings unless specific hedge accounting criteria are met. For cash flow hedges, changes in the fair value of the derivative instrument are recognized in net earnings in the same period as the hedged item and any changes in the fair value prior to that period are recognized in other comprehensive income. For fair value hedges, both the derivative instrument and the underlying commitment are recognized on the balance sheet at their fair value and any changes in the fair value are recognized currently in net earnings. The Company's foreign exchange contracts have been accounted for as cash flow hedges.

Under U.S. GAAP, SFAS 133 would result in an increase in total assets of \$192 as of December 31, 2005 (\$179 as of December 31, 2004) related to the fair value of the Company's foreign exchange contracts.

### **iv) *Investment in Joint Ventures***

The accounts of the Company's 49% joint venture interest in Point and former 48.7% joint venture interest in Mezure, Inc. (prior to the Company acquiring a 74% controlling interest on July 23, 2001) are proportionately consolidated as required under Canadian GAAP. Under U.S. GAAP, proportionate consolidation is not permitted, and the Company's investment in these joint ventures would be accounted for using the equity method. As permitted by SEC guidance, the effects of this difference in accounting principles have not been reflected in the accompanying tables.

In 2002, the Company recognized a gain of \$121 related to the reduction of its equity interest in Mezure from approximately 74% to 70%. Under U.S. GAAP, the Company would have reflected the effects of this transaction as a direct increase in shareholders' equity of \$160 after consideration of the impact of previous U.S. GAAP adjustments.

In addition, in 2003, the Company recognized a gain of \$379 related to the liquidation of the remaining assets and liabilities of Mezure. Under U.S. GAAP, this gain would have been \$571, since \$192 characterized as goodwill under Canadian GAAP would have been expensed on acquisition in 2001 (see Note (i) above).

**v) Intangibles Related to Acquisition of CMC Electronics' OEM GPS Business**

On May 14, 2003, the Company acquired the CMC Electronics non-aviation GPS product line. The fair value of the net assets acquired included \$497 in intangibles, comprised primarily of technology, product design, customer relationships and an established market presence. Under U.S. GAAP, when accounting for transfer of assets between entities under common control, the entity that receives the net assets or the equity interest would initially recognize the assets and liabilities transferred at their carrying amounts at the date of transfer. Any excess of consideration given over the controlling shareholders' carrying value would be accounted for as a reduction of equity.

**vi) Classification of Employee Relocation and Termination Costs**

In the year ended December 31, 2002, the Company included \$128 of employee relocation and \$84 of employee termination costs within other expense in the consolidated statement of operations. Under U.S. GAAP, these costs would be included within operating expenses.

**vii) Provision for Future Warranty Costs**

The changes in the provision for future warranty costs during each of the five years ended December 31, are as follows:

	<u>2005</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>	<u>2001</u>
Opening balance, beginning of period .....	\$ 538	\$ 410	\$ 344	\$ 285	\$ 268
Additions to provision .....	382	312	220	203	148
Costs incurred .....	<u>(227)</u>	<u>(184)</u>	<u>(154)</u>	<u>(144)</u>	<u>(131)</u>
Ending balance, end of period ..	<u>\$ 693</u>	<u>\$ 538</u>	<u>\$ 410</u>	<u>\$ 344</u>	<u>\$ 285</u>

**viii) Investment Tax Credits**

Under Canadian GAAP, the Company uses the cost reduction method to account for its investment tax credits. The investment tax credits relate to certain research and development expenses and are recognized when there is reasonable assurance that the Company will be able to realize the benefit of these credits. In the year ended December 31, 2005, the Company recognized \$1,756 (\$4,356 in 2004, \$nil in 2003) of investment tax credits, of which \$1,592 was recorded on the statement of operations as a benefit of prior years' investment tax credits on the statement of operations and \$164 was recorded as a reduction of deferred development costs on the balance sheet.

Under U.S. GAAP, the Company would use the flow through method to account for its investment tax credits and would record the recognition of the \$1,756 of investment tax credits in 2005 as a reduction of the current income tax provision. Under U.S. GAAP, for the year ended December 31, 2004, the Company would record the recognition of the \$4,356 of investment tax credits as a \$2,258 reduction of the current income tax provision and as a \$2,098 increase in future income tax benefit.

The net effect of these reconciling items would be an increase in net income from continuing operations of \$164 in the year ended December 31, 2005 under U.S. GAAP.

**ix) Comprehensive Income**

U.S. GAAP utilizes the concept of comprehensive income, which includes net income and other comprehensive income. Currently, there is no similar concept under Canadian GAAP. Other comprehensive income represents the change in equity during the period from transactions and other events from non-owner sources and includes such items as changes in the fair value of cash flow hedges.

**x) Summary of the Differences between Canadian and U.S. GAAP**

The effects of the above-noted differences between U.S. and Canadian GAAP produces the following differences on the presented statement of operations data:

	Year Ended December 31,				
	2005	2004	2003	2002	2001
<b>Net income from continuing operations —</b>					
<b>Canadian GAAP</b> .....	\$16,716	\$12,794	\$3,100	\$2,145	\$ 1,066
Adjustments to U.S. GAAP					
Deferred development costs (i) .....	—	(218)	(157)	(125)	(4)
Amortization of deferred development costs (i) .....	538	416	196	57	36
Stock-based compensation expense (ii) .....	587	326	—	—	—
Reduction of deferred development costs related to recognition of investment tax credits ..	164	—	—	—	—
Amortization of intangibles acquired from CMC Electronics (v) .....	124	124	62	—	—
<b>Net income from continuing operations —</b>					
<b>U.S. GAAP</b> .....	<u>18,129</u>	<u>13,442</u>	<u>3,201</u>	<u>2,077</u>	<u>1,098</u>
Net income (loss) from discontinued operations — Canadian GAAP .....	—	21	360	(648)	(956)
Adjustments to U.S. GAAP					
Gain on liquidation of Mezure, Inc. (iv) .....	—	—	192	—	—
Gain on dilution of equity in Mezure, Inc. (iv) .....	—	—	—	(121)	—
Write-off of Mezure, Inc. development related costs (i) .....	—	—	—	—	(231)
Income (loss) from discontinued operations — U.S. GAAP .....	<u>—</u>	<u>21</u>	<u>552</u>	<u>(769)</u>	<u>(1,187)</u>
<b>Net income (loss) — U.S. GAAP</b> .....	<u>18,129</u>	<u>13,463</u>	<u>3,753</u>	<u>1,308</u>	<u>(89)</u>
Net unrealized gain (loss) on foreign exchange contracts (iii) .....	192	179	—	(48)	1
Reclassification to income of gains and losses on cash flow hedges .....	(179)	—	48	(1)	—
<b>Comprehensive income (loss)</b> .....	<u>\$18,142</u>	<u>\$13,642</u>	<u>\$3,801</u>	<u>\$1,259</u>	<u>\$ (88)</u>

Net income (loss) per share as computed under Canadian and U.S. GAAP is as set forth below for the following periods:

	Year Ended December 31,				
	2005	2004	2003	2002	2001
<b>Net income per share from continuing operations</b>					
Canadian GAAP — basic .....	\$2.01	\$1.59	\$0.40	\$0.28	\$0.14
U.S. GAAP — basic .....	\$2.18	\$1.67	\$0.41	\$0.27	\$0.14
Canadian GAAP — diluted .....	\$1.91	\$1.51	\$0.39	\$0.27	\$0.14
U.S. GAAP — diluted .....	\$2.07	\$1.58	\$0.40	\$0.27	\$0.14

	Year Ended December 31,				
	2005	2004	2003	2002	2001
<b>Net income (loss) per share</b>					
Canadian GAAP — basic .....	\$2.01	\$1.59	\$0.45	\$0.19	\$ 0.01
U.S. GAAP — basic .....	\$2.18	\$1.67	\$0.49	\$0.17	\$(0.01)
Canadian GAAP — diluted .....	\$1.91	\$1.51	\$0.43	\$0.19	\$ 0.01
U.S. GAAP — diluted .....	\$2.07	\$1.58	\$0.47	\$0.17	\$(0.01)

The reconciliation of the selected consolidated financial data between U.S. and Canadian GAAP produces the following differences on the presented balance sheet data:

	Year Ended December 31				
	2005	2004	2003	2002	2001
<b>Total Assets</b>					
Canadian GAAP .....	\$71,255	\$52,946	\$35,572	\$30,890	\$27,821
Adjustments to U.S. GAAP					
Deferred development costs (i) .....	(1,657)	(2,359)	(2,557)	(2,596)	(2,528)
Fair value of financial instruments (iii) .....	192	179	—	(48)	—
Write off of development related costs on					
Mezure acquisition (i)(iv) .....	—	—	—	(192)	(231)
Reduction of intangibles acquired from					
CMC Electronics to carrying value (v) .....	(182)	(306)	(430)	—	—
U.S. GAAP .....	<u>\$69,608</u>	<u>\$50,460</u>	<u>\$32,585</u>	<u>\$28,054</u>	<u>\$25,062</u>
<b>Total Shareholders' Equity</b>					
Canadian GAAP .....	\$58,117	\$40,093	\$25,447	\$20,547	\$19,086
Adjustments to U.S. GAAP					
Deferred development costs (i) .....	(1,657)	(2,359)	(2,557)	(2,596)	(2,528)
Write off of development related costs on					
Mezure acquisition (i)(iv) .....	—	—	—	(192)	(231)
Reduction of intangibles acquired from					
CMC Electronics to carrying value (v) .....	(492)	(492)	(492)	—	—
Amortization of intangibles acquired from					
CMC Electronics (v) .....	310	186	62	—	—
U.S. GAAP before other comprehensive income ....	<u>\$56,278</u>	<u>\$37,428</u>	<u>\$22,460</u>	<u>\$17,759</u>	<u>\$16,327</u>
Accumulated other comprehensive					
income (loss) .....	192	179	—	(48)	1
U.S. GAAP including accumulated					
comprehensive income .....	<u>\$56,470</u>	<u>\$37,607</u>	<u>\$22,460</u>	<u>\$17,711</u>	<u>\$16,328</u>

(b) Canadian and U.S. Dollar Exchange Rate

The following table sets forth, for each period presented, the high, low and average exchange rates during the indicated period and the exchange rates at the end of the indicated period for one Canadian dollar, expressed in U.S. dollars, based on the noon buying rate in New York City for cable transfers payable in Canadian dollars as certified for customs purposes by the Federal Reserve Bank of New York:

U.S. Dollars Per Canadian Dollar Year Ended December 31					
	2005	2004	2003	2002	2001
Average .....	\$0.8254	\$0.7682	\$0.7139	\$0.6368	\$0.6457
High .....	0.8690	0.8493	0.7738	0.6619	0.6697
Low .....	0.7872	0.7158	0.6349	0.6200	0.6241
Period end .....	0.8579	0.8310	0.7738	0.6329	0.6267

Month Ended						
	April 2006	March 2006	February 2006	January 2006	December 2005	November 2005
High .....	\$0.8936	\$0.8834	\$0.8788	\$0.8744	\$0.8690	\$0.8579
Low .....	\$0.8534	\$0.8531	\$0.8638	\$0.8528	\$0.8521	\$0.8361

On May 4, 2006 the exchange rate was U.S. \$0.9037 per CDN \$1.00.

(c) Dividends

The Company has not paid any cash dividends since its inception. The Board of Directors may pay cash dividends in the foreseeable future, but intends to retain the majority of earnings, if any, for use in its business operations.

**B. Capitalization and Indebtedness**

Not applicable.

**C. Reasons for the Offer and Use of Proceeds**

Not applicable.

**D. Risk Factors**

*In addition to the other information set forth in this Annual Report, the following risk factors should be considered carefully in evaluating the Company. This Annual Report contains certain forward-looking statements and intentions. The cautionary statements made in this Annual Report should be read as being applicable to all related forward-looking statements wherever they appear in this Annual Report. The Company's actual results could differ materially from those discussed here. Factors that could cause or contribute to such differences include those discussed below, as well as those discussed elsewhere in this Annual Report.*

*The Company's operating results are susceptible to fluctuations.*

NovAtel's results of operations have fluctuated and can be expected to continue to fluctuate on a periodic basis as a result of a number of factors which affect revenue, gross margin and operating expenses. Annual and quarterly revenues have fluctuated because of a number of factors, including fluctuations in demand for existing products, the rate of development of new products, the degree of market acceptance of new products, increased competition, acquisition of new product lines, timing of major contracts, U.S. dollar to Canadian dollar exchange rates, operating results of subsidiaries and joint ventures, certification and market acceptance of new products, impact and timing

of large orders, pricing pressures in the market, establishing and maintaining effective distribution channels, fluctuations in non-recurring engineering ("NRE") fees, seasonality and other factors affecting customer purchase patterns and the timing of industry trade shows.

Gross margin as a percentage of revenue varies primarily as a result of product sales mix, the proportion of total revenue comprised of NRE revenue, changes in materials and contract manufacturing costs, liquidation of discontinued inventory, and absorption of fixed manufacturing costs.

A shortfall from anticipated revenue, lower gross margins or higher than expected expenses could adversely affect results of operations. In addition, if NovAtel were to receive a major contract, the Company's expenditures required to support such a contract would likely increase. If revenue from the contract were delayed for any reason, including cancellation or deferral of the contract, the Company's results of operations could be adversely affected. See "Item 5 — Operating and Financial Review and Prospects, Operating Results."

*If the Company's product innovations and enhancements are not successful, the Company's revenue growth and results of operations may be adversely impacted.*

Although NovAtel expects to make significant investments in research and development to continue to enhance existing products, develop new products which incorporate new and existing technologies and achieve market acceptance for such products, there can be no assurance that such new products or product enhancements will be successfully developed or, if developed, that any such new products or product enhancements will be developed in time to capture market opportunities or achieve a significant or sustainable level of market acceptance in new and existing markets. The development of new, technologically advanced products and product enhancements is a complex and uncertain process requiring accurate anticipation of technological and market trends. Any inability on NovAtel's part to successfully define, develop and introduce new products and product enhancements may materially adversely affect its growth potential and results of operations.

In addition, development and manufacturing schedules for technology products are difficult to predict, and there can be no assurance that NovAtel will achieve timely initial customer shipments of new products. The timely availability of these products in the market place and their acceptance by customers are important to the future success of NovAtel. NovAtel has previously experienced delays in shipping certain of its products and any future delays, whether due to manufacturing delays, product design and development delays, lack of market acceptance, delays in any required regulatory approval, or otherwise, could adversely affect customer acceptance of its products and have a material adverse effect on NovAtel's business, financial condition and results of operations. From time to time, NovAtel or its competitors may announce new products, capabilities or technologies that have the potential to replace or shorten the life cycles of its existing products. No assurance can be given that announcements of currently planned or other new products will not cause customers to defer or stop purchasing NovAtel products until NovAtel or its competitors' new products become available. In addition, certain of NovAtel's products must pass governmental and similar certifications before they can be sold. Any inability or delay in obtaining such certifications could have a material adverse effect on NovAtel's business, financial condition and results of operations. See "Item 4 — Information on the Company, Business Overview — Research and Development."

*The Company is subject to exchange rate fluctuations which could have a material effect on the Company's revenues and results of operations.*

Over 95% of NovAtel's revenues have been, and are likely to continue to be, realized in currencies other than the Canadian dollar, principally the U.S. dollar. A significant portion of NovAtel's expenses, however, will be incurred in Canadian dollars. Accordingly, fluctuations in the exchange rates between the U.S. dollar and other foreign currencies and the Canadian dollar could have a material adverse effect on NovAtel's revenues and its results from operations. If the Canadian dollar increases in value relative to the U.S. dollar, NovAtel's reported Canadian dollar revenues and net income may be materially and adversely affected. For example, during 2005, the Canadian dollar increased in value relative to the U.S. dollar from \$0.8310 on January 1, 2005 to \$0.8579 on December 31, 2005. NovAtel uses forward foreign currency contracts to hedge a portion of its exposure to fluctuations in the U.S. dollar and Euro. There can be no assurance that NovAtel will be successful in such hedging activities.

*The Company relies on a limited number of customers for a substantial portion of its revenue and any loss of any key customer could have a material effect on the Company's business, financial condition or results of operations.*

In 2005, the Company derived 49% of its revenues from its top four customers, namely Leica Geosystems A.G. ("Leica Geosystems"), Beijing BDStar, Raytheon Company ("Raytheon"), and Sokkia Co. Ltd. ("Sokkia")/Point. The loss of any key customer could have a material adverse effect on the Company's business, financial condition and results of operations. In addition, should any of the Company's customers experience financial difficulties resulting in an inability to pay amounts owing to the Company, the Company may experience a material adverse effect on its financial condition and results of operations.

The Company's strategic co-operation agreement with Leica Geosystems provides that in the event of the acquisition of control of NovAtel or a significant portion of its assets by certain specified competitors of Leica Geosystems, then Leica Geosystems may, among other things, terminate the agreement and any related development or supply agreements. The strategic co-operation agreement between the Company and CMC Electronics contains a similar right in favour of CMC Electronics which is triggered in circumstances in which control of NovAtel or a significant portion of its assets are acquired by certain specified competitors of CMC Electronics. The termination of either of such agreements could have a material adverse effect on NovAtel's business, financial condition and results of operations and could cause the Company's quarterly operating results to fluctuate and cause its stock price to decline.

*The Company places binding manufacturing orders based on its forecasts and, if the Company fails to adequately forecast demand for its products, it may incur product shortages or excess product inventory.*

The Company's third-party manufacturers require the Company to place binding manufacturing orders in advance of the Company receiving purchase orders from its customers. This may result in product shortages or excess product inventory because the Company cannot easily increase or decrease these purchase orders. Obtaining additional supply in the face of product shortages may be costly or impossible, particularly in the short term, which could prevent the Company from fulfilling orders. If the Company fails to adequately forecast demand for its products it could cause the Company's operating results to fluctuate and cause its stock price to decline.

*The Company relies on suppliers for the components used in its products and interruptions in the supply of such components or a significant increase in the price of one or more components could adversely affect the Company's business, financial condition and results of operations.*

Most of the components used in the Company's products are standard parts readily available from more than one supplier. However, a few components are sourced from sole suppliers or are custom parts unique to NovAtel, including application specific integrated circuits manufactured to proprietary design, radio frequency filters, microprocessors and duplexers/filters. While custom parts make the Company's products hard to imitate, they also represent a manufacturing risk due to the lack of alternative suppliers. If these parts became unavailable, redesign or modification of the Company's products could be required. In addition, suppliers may cease manufacturing common components, replacing them with newer parts, which require requalification. These risks could cause an interruption in the Company's ability to provide a steady stream of products to its customers, which would adversely impact the Company's revenues and results of operations.

NovAtel has experienced significant production delays in the past caused by an insufficient supply of certain components. If NovAtel is unable to obtain a sufficient supply of single source components from its current vendors, NovAtel may be required to obtain such components from alternative sources at higher prices and may experience a delay or interruption in product shipments, which could adversely affect its business, financial condition and results of operations and damage customer relationships until an alternative source can be obtained. NovAtel has taken steps to ensure adequate supply of these components and commenced product redesigns, as may be required.

Also, a significant increase in the price of one or more components could adversely affect NovAtel's business, financial condition and results of operations. Although NovAtel has instituted vendor audit programs, there can be no



assurance that NovAtel will not face problems with the quality of components in the future that could result in delays in supplies, interrupt shipments and require modification of products already sold by NovAtel, any of which could have a material adverse effect on NovAtel's business, financial condition and results of operations. NovAtel currently relies on two primary subcontractors to manufacture the majority of its circuit card assemblies. There can be no assurance that the circuit card assembly subcontractors will be able to manufacture NovAtel's products in a timely and reliable manner. The failure by a subcontractor to manufacture products in a timely and reliable manner could have a material adverse effect on NovAtel's business, financial condition and results of operations.

*The Company's success is dependent upon key personnel.*

NovAtel's future success depends, in part, on its ability to attract and retain qualified technical staff, such as geomatics engineers, electrical engineers (including radio frequency engineers, A.S.I.C. engineers and digital signal processing engineers), printed circuit board technologists, marketing, sales and executive management. Competition for such personnel is intense and the number of persons with relevant experience, particularly in engineering, is limited. Any inability on the part of NovAtel to attract and retain additional key employees or the loss of one or more of its current key employees could materially adversely affect NovAtel's business, financial condition and results of operations.

*The Company may not be able to maintain existing OEM customers and strategic relationships or develop distribution channels for the sale of its products which would affect the Company's revenues and results of operations.*

NovAtel sells its OEM products directly to OEM customers and to strategic relationships. The Company expects to continue to utilize these relationships to sell to companies that will incorporate NovAtel's products into their products and services. Accordingly, the Company's success will be dependent in large part on its ability to continue existing relationships and develop new OEM and other third party relationships.

NovAtel cannot predict nor control the extent to which its distribution network will be successful in marketing products incorporating the Company's technology. A material loss of any of the Company's key OEM customers or strategic partners, either as a result of competitive products offered by other companies or products developed internally by these OEM customers and strategic partners, or their inability to penetrate their respective market segments, could have a material adverse effect on the Company's business, financial condition and results of operations. There can be no assurance that NovAtel can continue to attract OEM customers, dealers and strategic partners and any inability to do so could materially adversely affect the Company's business, financial condition and results of operations.

NovAtel plans to continue expanding its distribution channels. There can be no assurance that such expansion will be successfully completed, that the cost of such expansion will not exceed the revenues generated, or that the Company's sales and marketing organization will be able to successfully compete against the more extensive and well-funded sales and marketing operations of many of NovAtel's current or potential competitors. NovAtel's inability to manage effectively its distribution expansion could have a material adverse effect on the Company's business, financial condition and results of operations. See "Item 4 — Information on the Company, Business Overview — Sales, Marketing and Distribution."

*The price of NovAtel's common shares has fluctuated substantially over the last few years.*

Since January 1, 2005, the price of NovAtel's common shares has ranged from a low of U.S. \$14.32 to a high of U.S. \$48.45. A number of factors will continue to influence the market price for the common shares, including:

- volume and timing of orders for NovAtel's products;
- quarterly variations in NovAtel's or its competitors' results of operations;
- the announcement and introduction of new products or product enhancements by NovAtel or its competitors;

- the announcement of acquisition of companies or technologies by NovAtel or its competitors;
- product liability claims or other litigation;
- changes in earnings estimates or recommendations by securities analysts; and
- general market conditions and other factors that may be unrelated to NovAtel's operating performance or the operating performance of its competitors.

If the trading market for NovAtel's stock does not continue to develop, securities analysts may not initiate or maintain research coverage of NovAtel and its shares, and this could adversely affect the market for NovAtel's shares.

*The Company may be adversely affected by trends in the markets for GPS technology and products.*

NovAtel currently addresses the following markets for the application of GPS technology: surveying and mapping, aerospace, precision agriculture, precise timing, marine, unmanned vehicles, mining and machine control. Although NovAtel believes that these markets have growth potential for sales of GPS products, there can be no assurance that such markets will continue to develop, particularly given that GPS-based systems are still in an early stage of adoption in some of these markets, or that even if they develop, such markets will develop in a direction beneficial to NovAtel's products or product positioning or in the time frame in which NovAtel expects to launch products for these markets. Any development of these markets away from GPS technologies or the GPS products offered by NovAtel could have a material adverse effect on NovAtel's growth potential and its business, financial condition and results of operations.

NovAtel also believes that in certain emerging markets its success will depend on its ability to form and maintain strategic relationships with established system providers and industry leaders. NovAtel's failure to form and maintain such relationships, or the pre-emption of such relationships by the actions of other GPS competitors, could adversely affect its ability to penetrate emerging GPS markets. In addition, NovAtel's future growth will depend upon the timely development of the markets in which it currently competes, its ability to continue to identify and exploit new markets for its products and its ability to open new channels of distribution for existing and future products. NovAtel's inability to effectively and efficiently exploit opportunities in new or emerging markets through successful product marketing, new and timely product introductions and product enhancements and establishing new distribution channels for its products could have a material adverse effect on NovAtel's growth, financial condition and results of operations. Further, to the extent NovAtel builds inventory in anticipation of potential sales in a new market, the failure of that market to develop could have a material adverse effect on NovAtel's business, financial condition and results of operations.

*The Company is working towards compliance with new European Union ("EU") restrictions on the use of certain hazardous substances, which may increase the Company's cost or limit the Company's ability to sell product in Europe.*

There are EU directives that restrict the use of certain hazardous substances and also create requirements on waste electrical and electronic equipment. NovAtel is currently planning to be compliant on both of these directives before the deadlines. However, if the Company's product development is delayed or if the Company is unable to locate suitable compliant parts and/or compliant manufacturing practices, which deliver the same level of quality as current practices, the Company's sales to Europe may be impacted, starting in July 2006. In addition, the Company may incur increased costs to dispose of obsolete inventory.

*The failure of Point to repay existing loans to the Company or continue as a going concern could adversely affect the Company's results of operations.*

NovAtel sells GPS receivers and antennas to Point which incorporates these receivers into surveying systems that are in turn sold through Sokkia's distribution channels and through independent dealers and distributors. NovAtel's consolidated financial statements include its proportionate 49% joint venture interest in the accounts of Point. Point is subject to similar types of risks as the Company.

Point is dependent on the Company and Sokkia for product supply, distribution and financing. As of December 31, 2005, the Company and Sokkia had collectively loaned Point U.S. \$5.3 million, U.S. \$2.6 million of which was advanced by the Company. The loans are secured by the assets of Point.

Should Sokkia and the Company discontinue their support, Point's ability to continue as a going concern would be impaired. If the existing loans were ultimately not repaid by Point to the Company and Sokkia, and/or if Point were liquidated in an orderly wind-down, the Company believes that its maximum loss exposure in the statement of operations to Point as of December 31, 2005, after consideration of the effects of the proportionate consolidation of Point, would be approximately \$600,000, comprised primarily of working capital related items and the costs that would be incurred to cease operations. The consolidated financial statements of the Company contained elsewhere in this Annual Report do not reflect any adjustments that would be required if Point's operations were discontinued. See "— Dependence on Key Customers."

*The Company's business is dependent on its intellectual property. If the Company's patents or trademarks are declared invalid, the Company's ability to compete may be adversely affected.*

NovAtel currently holds 30 U.S. patents and various related foreign patents which expire at various dates no earlier than November 28, 2010. NovAtel also has numerous pending U.S. and foreign patent applications. NovAtel currently licences certain peripheral aspects of its technology from third parties. Although NovAtel believes that its patents and trademarks have value, there can be no assurance that its patents and trademarks, or any additional patents and trademarks that may be obtained in the future, will provide meaningful protection from competition. The value of NovAtel's products relies substantially on its technical innovation in fields in which there are many current patent filings. NovAtel recognizes that as new patents are issued or are brought to its attention by the holders of such patents, it may be necessary for NovAtel to withdraw products from the market, negotiate a license from such patent holders, redesign its products or pay damages assessed as a result of litigation. Such events could have a material adverse effect on NovAtel's business, financial condition and results of operations. In addition, the legal costs and engineering time required to safeguard intellectual property or to defend against litigation could become a significant expense of operations.

NovAtel has received written notices from certain parties alleging patent infringement of their respective patents. Other than one claim by Trimble Navigation Limited ("Trimble") for which a settlement agreement was reached, to date, no formal claim has been brought by any of the parties. The Company believes it has valid defences to these claims should formal proceedings be commenced. In protecting its intellectual property rights NovAtel has from time to time sent out letters to third parties regarding potential infringement. While no intellectual property right of the Company has been invalidated or declared unenforceable, there can be no assurance that such rights will not be invalidated due to the existence of prior art or otherwise held unenforceable. See "Item 4 — Information on the Company, Business Overview — Legal Proceedings."

*The Company's acquisition strategy involves a number of risks, including overpayment, failure to adequately integrate an acquired business and distraction of management from core operations.*

In order to assist in the achievement of growth, NovAtel continues to seek acquisition opportunities to complement its existing businesses. NovAtel cannot be certain that it will be able to identify suitable acquisition candidates available for sale at reasonable prices, to consummate any acquisition, or to integrate any acquired business into its operations successfully. Acquisitions may involve a number of special risks, circumstances or legal liabilities, some or all of which may have a material adverse effect on NovAtel's business, results of operations and financial condition. Acquisitions may also result in potentially dilutive issuances of equity securities. When evaluating an acquisition opportunity, NovAtel cannot be certain that it has correctly identified and managed the risks and costs inherent in the business that it is acquiring.

From time to time, NovAtel engages in discussions and activities with respect to possible acquisitions. At any given time, discussions and activities can be in process on a number of initiatives, each at different stages of development. While at the present time NovAtel has no binding agreement or commitment to enter into any such transaction, in normal

course, from time to time, it pursues potential acquisitions. NovAtel can provide no assurance that any potential transaction will be successfully completed, and, if completed, that the business acquired will be successfully integrated into NovAtel's operations. The failure of NovAtel to manage its acquisition strategy successfully could have a material adverse effect on NovAtel's business, results of operations and financial condition.

*The products and services provided by the Company could expose the Company to product liability and other claims.*

There is a risk that NovAtel's products and services may not perform up to expectations. While NovAtel usually contractually limits its liability for damages arising from its provision of services, there can be no assurance that the contractual limitations will be enforceable in all circumstances or in all jurisdictions. Furthermore, litigation, regardless of contractual limitations, could result in substantial cost to NovAtel, divert management's attention and resources from NovAtel's operations and result in negative publicity that may impair its ongoing marketing efforts. Although NovAtel has general liability insurance, there is no assurance that this insurance will cover the claims or that the claims will not exceed the insurance limit under its current policies.

*The Company's business may be adversely affected by risks associated with international operations.*

NovAtel derives a significant portion of its revenues from international sales. NovAtel plans to continue to expand its international sales and marketing efforts. There are a number of risks inherent in NovAtel's international business activities, including unexpected changes in Canadian, United States or other government policies concerning the import and export of goods, services and technology and other regulatory requirements, tariffs and other trade barriers, costs and risks of localising products for foreign countries, higher credit risks, potentially adverse tax consequences, limits on repatriation of earnings and the burdens of complying with a wide variety of foreign laws. Fluctuations in currency exchange rates could materially adversely affect sales denominated in currencies other than the Canadian dollar and cause a reduction in revenues derived from sales in a particular currency. The financial stability of foreign markets could also affect the Company's international sales. There can be no assurance that such factors will not materially adversely affect the revenues from NovAtel's future international sales and, consequently, its results of operations. In addition, revenues that NovAtel earns abroad may be subject to taxation by more than one jurisdiction, which could materially adversely affect its earnings. Furthermore, in certain foreign markets, there may be a reluctance to purchase products based on GPS technology, given the control of GPS by the U.S. Government. Each of these factors could have an adverse effect on NovAtel's business, financial condition and results of operations. See "Item 4 — Information on the Company, Business Overview — Sales, Marketing and Distribution."

*The adoption of new technologies to replace GPS could adversely affect the Company's business.*

The Company operates in a highly technical market. Technology is constantly advancing and changing to meet new demands. NovAtel is unable to determine if GPS will be essential in the future due to unpredictable advances in technology. There is a risk that GPS may be replaced with entirely new technologies and products which are not foreseeable at this time.

*Competition and increased industry consolidation could adversely affect the Company's business, financial condition and results of operation.*

The GPS industry has been going through a consolidation phase over the past several years. A number of GPS companies have been selecting strategic partners to merge, acquire or form joint businesses in an effort to remain cost competitive and meet customer requirements. The Company expects that this consolidation phase will continue for the foreseeable future resulting in fewer, but larger companies. Industry consolidation, by creating stronger and larger potential competitors, could have a material adverse effect on the Company's business, financial condition and results of operations. See "Item 4 — Information on the Company, Business Overview — Competition."

*A disruption of the GPS satellite network or governmental regulation of this network or GPS products could impair the viability of the Company's business.*

The Company's products rely on signals from GPS satellites and to a lesser extent GLONASS and Galileo satellites. GPS satellites and their ground support systems are complex electronic systems subject to electronic and mechanical failures and possible sabotage. As of March 2006, there are 29 usable satellites, five more than the design requirement. The satellites have a limited design life of between seven and 11 years and the satellites are also subject to damage by the hostile space environment in which they operate. Of the current constellation of satellites, 19 are past their design target and five are past their design life target by six years or more. The repair of damaged or malfunctioning satellites is nearly impossible. If a significant number of satellites were to become inoperable, there could be a substantial delay before they are replaced with new satellites. A reduction in the number of operating satellites would impair the current usefulness of the GPS system or the growth of current and additional market opportunities, which, in either case, would adversely affect the Company's business, financial condition and the results of operations. Spare satellites have been launched to address these concerns. There can be no assurance that the U.S. Government will remain committed to the operation and maintenance of GPS satellites over a long period of time, or that the policies of the U.S. Government for the use of GPS without charge will remain unchanged.

Prior to May 2000, the accuracy of GPS was reduced by the distortion of GPS signals as a result of selective availability ("SA"), which was controlled by the U.S. Department of Defense. SA was the activated, intentional system-wide degradation of stand alone GPS accuracy from approximately 25 metres to approximately 100 metres. The Department of Defense implemented SA in order to deny hostile forces accurate position, time and velocity information supplied by GPS. In certain military applications, classified devices are utilized to decode the SA degradation and return accuracies to their original levels. NovAtel has to date been able to design products that will reduce the degradation that can be caused by SA. Although the U.S. Government discontinued the use of SA effective May 2000, there can be no assurance that the U.S. Government will not take further actions which would adversely affect the use of GPS. These actions could include various methods of degrading the system, rendering it inoperable or the re-implementation of SA by the U.S. Department of Defense in times of military action. There can be no assurances that NovAtel would be able to design products to compensate for these further actions. In addition, to protect national security interests, various U.S. Government agencies have indicated their intention to limit or prohibit the use of techniques which compensate for SA and such limitations or prohibitions could have a material adverse effect on the Company's business, financial condition and results of operations. Certain non U.S. government organizations have expressed concern regarding the susceptibility of GPS equipment to intentional or inadvertent signal interference. Such concern could translate into reduced demand for GPS products in certain geographic regions.

The European Community and European Space Agency have completed plans and are in the process of launching full-scale development of Galileo, a system similar in capability to GPS. NovAtel is actively involved in Galileo receiver development activities under contracts funded by the Canadian Space Agency and the European Space Agency. There can be no assurance that NovAtel will be able to design products compatible with Galileo or that external funding will continue to be available for such work.

*The Company derives a substantial portion of its revenue from the aviation industry and factors that adversely affect the aviation industry generally could adversely affect the Company's financial condition and results of operations.*

NovAtel derives revenue from the Aerospace and Defence market sector, a substantial portion of which has been derived from sales to the ground and airborne aviation industry. In the past four and a half years, the aviation industry has experienced an economic slow down and recently began to recover from activities arising from the events of September 11, 2001 in the United States. In addition, as of December 31, 2005, NovAtel deferred \$1.7 million of costs related to the development of a certified aviation GPS receiver. A protracted downturn in the aviation industry could result in a material adverse effect on the Company's revenue from this market and NovAtel's ability to recover the deferred development costs which could adversely affect its financial condition and results of operations.

*The Company may be unable to utilize certain tax deductions and investment tax credits, which could adversely affect the Company's results of operations.*

The Company's operations are substantially located in Canada and accordingly, Canada is the Company's main tax jurisdiction. The Company has not recorded a provision for current income taxes in Canada, other than for Canadian federal large corporations tax, income tax related to Waypoint's operations prior to amalgamation with NovAtel and a provision related to the benefit of income tax credits, due to previously incurred losses, credits and costs. As of December 31, 2005, the Company had approximately \$140 million of losses, investment tax credits, depreciation and research and development costs that are available to reduce future taxable income and taxes payable primarily in Canada. The Company has determined that the acquisition of a majority of its Common Shares by CMC Electronics in 1998, BAE SYSTEMS p.l.c.'s acquisition of the majority of the common shares of CMC Electronics in November 1999 and ONCAP's acquisition of the majority of the common shares of CMC Electronics in April 2001 each constitute an acquisition of control of the Company for Canadian income tax purposes. Accordingly, the availability of certain of the Company's Canadian income tax losses, research and development costs, depreciation deductible for tax purposes and investment tax credits may be subject to limitation. The ultimate availability and amount of these losses, credits and costs may be dependent upon future Canada Revenue Agency audits.

*NovAtel may incur significant costs to satisfy regulatory requirements relating to internal controls over financial reporting.*

Section 404 of the Sarbanes-Oxley Act of 2002 requires NovAtel to perform an evaluation of its internal controls over financial reporting and have its auditor attest to such evaluation. Currently, this evaluation will be required in the Company's Form 20-F for the fiscal year ending December 31, 2006. During 2006, NovAtel will be performing the system and process evaluation and testing (and any necessary remediation) required in an effort to comply with the management certification and auditor attestation requirements. As a result, the Company expects to incur additional expenses and diversion of management's time. While NovAtel currently anticipates being able to fully implement the requirements relating to internal controls and all other aspects of Section 404 in a timely fashion, the Company cannot be certain as to the timing of completion of its evaluation, testing and remediation actions or the impact of the same on its operations.

*The Company may be subject to litigation and infringement claims that may harm its business or reputation, be costly and divert management's attention.*

The technology used by NovAtel in its business may subject the Company to claims that the Company infringes on the patents or proprietary rights of others. The risk of this occurring will tend to increase as the GPS, GLONASS and Galileo industry expands and more patents are issued. Furthermore, many of the Company's competitors and other companies have already applied for patents covering technology similar to that used by the Company, and many patents have already been issued which cover these technologies. The Company may be involved in future lawsuits alleging patent infringement, other intellectual property rights violations, product liability claims or general commercial claims. In addition, litigation may be necessary to:

- assert claims of infringement;
- enforce the Company's patents, if any;
- protect the Company's trade secrets or know-how; and
- determine the enforceability, scope and validity of the proprietary rights of others.

The Company may be unsuccessful in defending or pursuing these lawsuits. Regardless of the outcome, litigation can be very costly, can divert management's efforts and could materially affect the Company's business and operating results. An adverse determination may subject the Company to significant liabilities or restrict or prohibit the Company from selling its products.

*The reallocation of radio frequency bands used by GPS technology or other interference with the reception of GPS signals could harm the utility and reliability of the Company's products.*

GPS technology is dependent on the use of the radio frequency spectrum. The assignment of spectrum is controlled by the International Telecommunications Union ("ITU"). The Federal Communications Commission ("FCC") and Industry Canada are responsible for the assignment of spectrum for non-government use in the United States and Canada, respectively, in accordance with ITU regulations. Any ITU, FCC or Industry Canada reallocation of radio frequency spectrum, including frequency band segmentation or sharing of the spectrum, could cause interference with the reception of GPS signals and may materially and adversely affect the utility and reliability of NovAtel's products, which would, in turn, have a material adverse effect on its business, financial condition and results of operations. In addition, emissions from mobile satellite service and other equipment operating in adjacent frequency bands or inband may materially and adversely affect the utility and reliability of NovAtel's products, which could result in a material adverse effect on the Company's business, financial condition and results of operations.

On May 11, 2000, the FCC issued a Notice of Proposed Rulemaking that proposed rules for the operation of Ultra Wideband ("UWB") radio devices on an unlicensed basis in the frequency bands allocated to GPS. A coalition of companies and trade associates, including various airline companies, the Air Transport Association of America and the U.S. GPS Industry Council, submitted a proposal for the regulation of UWB devices to the FCC in November 2001. On February 14, 2002, the FCC approved the commercial use of UWB technology at conservative power limits. The current standards of operation set limits on what radio frequencies UWB devices can be operating in, including avoiding those frequencies used by the military and companies that sell global positioning services. In February 2003, the FCC upheld its ruling to allow the production of UWB devices with "conservative" power limits. This may lead the way for a proliferation of personal wireless devices that would be manufactured and sold on the open market without licence requirements. No restrictions on the density of these devices will be defined. Therefore, it is possible that the GPS noise floor could be contaminated and rise by as much as 10 times the current level when operating in an area with a high density of operating UWB devices. This degradation of the GPS signal-to-noise ratio would adversely affect the performance of the receivers. NovAtel is adding additional digital signal processing algorithms to its next generation GPS receivers to enable tracking of weak GPS signals or continue to operate in high noise floor environments. If the FCC expands or changes the current UWB standards, UWB devices might cause interference with the reception of GPS signals. Such interference could reduce demand for GPS products in the future. Any resulting change in market demand for GPS products could have a material adverse effect on the Company's business, financial condition and results of operations.

*The Company may be unable to properly manage the discontinuation of its older products.*

As NovAtel develops newer products, many of its older products will reach their end of life. As NovAtel discontinues the manufacturing and sale of these older products, it must manage the liquidation of inventory, supplier commitments and customer expectations. If NovAtel is unable to properly manage the discontinuation of these older products, it could have a material adverse effect on its business, financial condition and results of operations.

#### **Item 4. Information on the Company**

##### **A. History and Development of the Company**

The Company was incorporated under the *Canada Business Corporations Act* ("CBCA") on October 17, 1978 as 89006 Canada Ltd. The Company was extra provincially registered in Alberta on November 20, 1979 and remains active in this jurisdiction as of the date of this Annual Report. In July 1979, the Company's name was changed to Westech Systems Ltd. and in April of 1983 was changed to NovAtel Communications Ltd. In October 1996, the Company changed its name to NovAtel Inc. and in November 1996, the Company amended its articles to split its then outstanding common shares from 4 million to 5.2 million and amended its articles to authorize the stated capital of the Company to include an unlimited number of Common Shares and First Preference Shares.

From the time of the Company's formation until the mid-1990s, NovAtel's business was focused on the development of various communication businesses based on wireless technology. In 1989, NovAtel acquired Norstar Instruments Ltd., a developer of GPS technology.

Between 1992 and 1996, NovAtel divested its non-GPS businesses in a series of transactions. Since that time, NovAtel's business has been focused primarily on high-precision GPS technology and products.

In 1997, NovAtel completed an initial public offering of its Common Shares in the United States and was concurrently listed on NASDAQ with the offering under the symbol "NGPS."

On April 17, 1998, pursuant to requests by its customers to integrate GPS technology into its aviation systems, CMC Electronics acquired 58.3% of the then outstanding Common Shares.

In 1999, Point was established to develop advanced measurement solutions that incorporate NovAtel's GPS technology, primarily for Sokkia's surveying and mapping markets.

On April 11, 2001, an investor group led by ONCAP L.P. ("ONCAP") acquired control of the Company through the acquisition of CMC Electronics.

In 2001, NovAtel acquired a controlling equity interest in Mezure, Inc. ("Mezure"), a company that had been developing a GPS, wireless communication and Internet-based product for deformation monitoring of man-made and natural structures. The business operations of Mezure were discontinued in 2003. See "Item 5 — Operating and Financial Review and Prospects, Operating Results — Overview."

In 2002, NovAtel and Leica Geosystems AG ("Leica Geosystems") formed a strategic partnership, under which NovAtel would develop and supply GPS-based products and technology to Leica Geosystems. See "Item 4 — Information on the Company, Business Overview — Strategic Partnerships — Leica Geosystems."

In May 2003, NovAtel acquired CMC Electronics' non-aviation L1 GPS OEM product line to broaden the Company's product line. See "Item 5 — Operating and Financial Review and Prospects, Operating Results — Overview."

In 2004, NovAtel and CMC Electronics formed a strategic partnership, under which NovAtel develops and supplies GPS-based products and technology to CMC Electronics. See "Item 4 — Information on the Company, Business Overview — Strategic Partnerships — CMC Electronics."

From January 2005 to August 2005, CMC Electronics sold all of its common shares of NovAtel.

On October 1, 2005, the Company acquired all of the shares of Waypoint Consulting Inc. ("Waypoint") for approximately \$3.5 million in cash, subject to post-closing adjustments to working capital. Waypoint's products include specialized real-time and post-processing GPS and GPS/inertial positioning and trajectory software. See "Item 5 — Operating and Financial Review and Prospects, Operating Results — Overview."

The Company's principal capital expenditures over the last three years were \$2.4 million in 2005, \$2.3 million in 2004 and \$2.7 million in 2003 and were primarily for equipment for research and development, computer equipment and software and patents/trademarks. The Company expects the capital expenditures of approximately \$5.0 million in 2006 to be internally financed.

NovAtel's Common Shares are listed on NASDAQ under the symbol "NGPS." The Company's head and registered offices are located at 1120-68th Avenue N.E., Calgary, Alberta, T2E 8S5, and its website is located at [www.novatel.com](http://www.novatel.com). The information on the website is not incorporated by reference into this Annual Report.

## **B. Business Overview**

### **General**

NovAtel designs, markets and sells high-precision GPS and other positioning components and sub-systems used in a wide variety of commercial applications principally in the aviation, geomatics (surveying and mapping), mining, precision agriculture, marine and defence industries. NovAtel's solutions combine hardware, such as



receivers and antennas, with software to enable its customers to fully integrate the Company's high-precision positioning technology into their respective products and systems. The Company is focused on supplying core high-precision positioning technology to OEMs and system integrators who build systems for various end market applications.

Management of the Company believes the primary customer benefits of NovAtel's core technology solutions include:

- high-precision positioning with accuracy to the sub centimetre level;
- high-reliability and robust performance, even in challenging environments;
- cost-effective components and sub-systems to enable broad market application;
- small, low-power designs for easy system integration; and
- flexibility to integrate customer software solutions enabling the Company's customers to reduce system costs and accelerate time to market.

The availability of reliable and cost-effective high-precision positioning technology has resulted in an expanding number of commercial applications for the technology. Examples of applications for this technology include enabling commercial aircraft to use direct point-to-point flight lines resulting in reduced operating cost, farmers to equip their tractors with machine controlled precision guidance systems, which typically results in lower operating costs and higher crop yields, and surveyors to use GPS-based instruments to survey sites more rapidly and accurately.

One of the most critical elements of the NovAtel solution is the Company's product line of GPS receivers. The receiver is the core technology which receives, processes and resolves the GPS signals. The majority of NovAtel's proprietary technology is incorporated into NovAtel's receivers and most of the research and development efforts of the Company are directed towards improving their accuracy, reliability and cost effectiveness. These receivers are highly flexible and configurable with software for differing accuracy and performance, allowing the Company and its customers to leverage a limited number of hardware platforms into a wide variety of end-market applications.

## **Industry Overview**

### ***Satellite Navigation Systems***

Location determination has become a fundamental requirement for many consumer and commercial activities. GPS is the world's most widely used and accepted technology for precise location determination.

Development of the GPS system began with the launch of the first GPS satellite in 1978. The GPS system was founded and continues to be funded and controlled by the U.S. Department of Defense. The purpose of the GPS system is to provide precise location and time determination for military and civilian applications. The GPS system can currently be accessed free of charge and provides positioning data 24 hours a day worldwide.

The survey industry was the first commercial market to make widespread use of the GPS system. Adoption began in the late 1980's and grew significantly in the early 1990's as new technologies emerged to make the applications more cost-effective. Since that time, use of the system has spread to a variety of commercial and consumer applications including navigation, tracking, mapping and monitoring.

The GPS system is based on signals presently provided by a constellation of 29 orbiting satellites. The system of satellites currently broadcasts on two frequencies, L1, which is available for civilian use, and L2 which is

encrypted and primarily used for military applications. GPS modernization will see a new frequency, L5, and a new Signal, L2C, on satellites launched in the future. GPS positioning is based on a triangulation technique that precisely measures the distance from a GPS receiver to satellites which continuously transmit precisely timed radio signals. GPS receivers calculate the distance by measuring the travel time of the satellite signal. Signals from four satellites are typically required to compute the three dimensional position of the GPS receiver. Under normal operating conditions, a receiver is able to receive signals from six to eight satellites at any point in time.

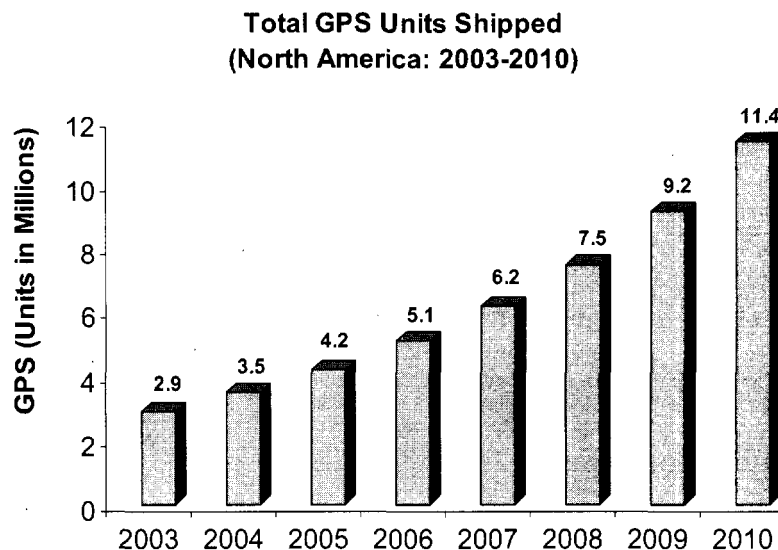
GLONASS is a similar positioning system established by the former Soviet Union and controlled and operated by the Russian government. The GLONASS system was introduced in 1982 with the launch of its first satellite and currently consists of 12 active satellites. Industry participants generally view GPS as being superior to GLONASS primarily as a result of the greater number of active satellites.

A third system, called Galileo, is currently being developed by the European Space Agency and is scheduled to become operational between 2008 and 2011. According to the report entitled "GPS World Markets" prepared by Allied Business Intelligence Inc., a leading industry research firm, and published in the fourth quarter of 2003 (the "Allied Report"), the European Union is planning to spend U.S. \$3.6 billion over the next several years to deploy the Galileo system. The development of alternative satellite positioning systems is a benefit to providers of global positioning technology, such as the Company, since products can be designed to use the signals from multiple systems resulting in greater accuracy and reliability.

### ***GPS Market Overview***

The market for positioning technology has experienced significant growth since the original launch of the first GPS satellites. According to the Allied Report, revenue from global GPS systems was estimated to be approximately U.S. \$15.0 billion in 2004. According to the report entitled "North American GPS Equipment Markets (A601-22)" prepared by Frost & Sullivan, a leading industry research firm, and published in 2004 (the "Frost & Sullivan Report", revenue from the North American GPS market was approximately U.S. \$4.1 billion in 2004 and is expected to grow to U.S. \$6.6 billion in 2007, a 17% compounded annual growth rate.

According to the Frost & Sullivan Report, total unit sales in the North American market are expected to grow from 2.9 million in 2003 to 11.4 million in 2010 for a compounded annual growth rate of approximately 22%. The following chart estimates total North American GPS units shipped or to be shipped for the periods indicated.

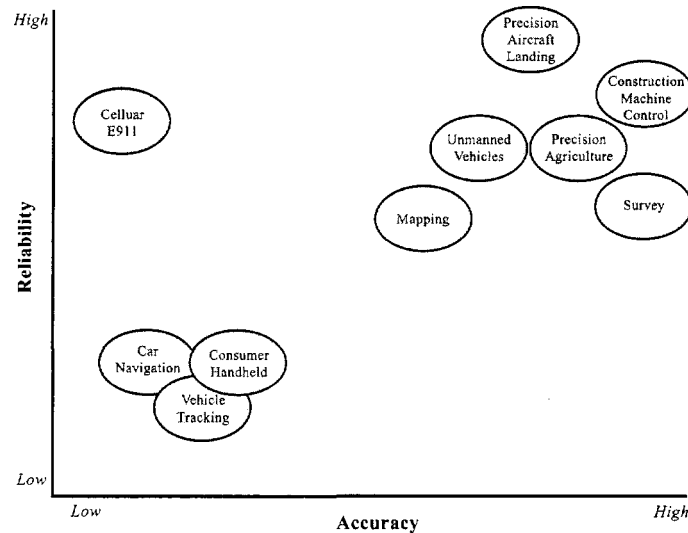


Source: Frost & Sullivan Report (2004).

## GPS Market

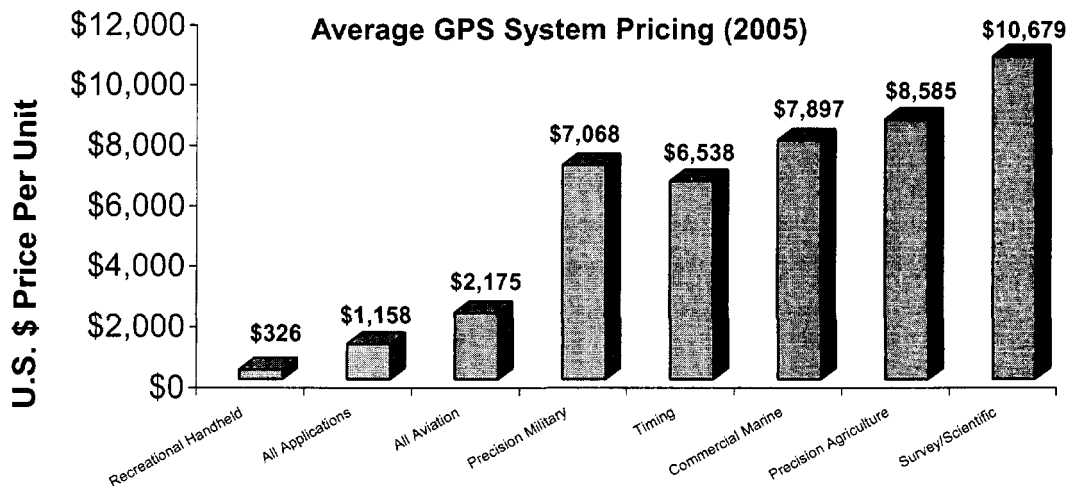
The overall GPS market can be divided into two primary segments, lower precision consumer markets and higher precision commercial markets. Management of the Company estimates NovAtel's current total addressable annual market for high-precision positioning component technologies and sub-systems is approximately U.S. \$300 million to U.S. \$400 million.

The following chart illustrates the view of management of the Company in respect of the relative accuracy and reliability needs of the various end-markets. Accuracy refers to how precise the positioning information is required to be in an application. Reliability refers to how important the continuity of positioning is to an application.



Management of the Company believes that a limited number of highly specialized GPS companies, including NovAtel, have the capability to develop and produce technology that can be used in higher precision applications, largely as a result of proprietary and patented technology.

As a result of the high degree of specialization required, commercial high-precision GPS component technology is typically sold at significantly higher prices, as illustrated by the following chart, which typically results in higher gross margins than lower precision, consumer focused systems.



Source: Frost & Sullivan Report (2004).

## ***Growth in High-Precision GPS***

Management of the Company believes that growth in the high precision segment of the GPS market is the result of an expanding number of applications which are being driven by technological advancements with respect to accuracy and reliability and a general reduction in the cost of peripheral component technology.

### ***Technological Advancements***

Since the introduction of GPS technology, there have been a number of technological innovations that have significantly increased the accuracy and reliability of GPS products. Differential GPS, one of the first techniques developed to improve performance, can be used to achieve position accuracies down to a few millimetres for certain applications. With this technique one receiver, typically called a base station, is precisely positioned on a known location and calculates a variety of measurement errors. This differential correction data is then broadcast via communication links to other receivers, that can be static or in motion, which receive the differential corrections and apply them to provide precise locations. Using this technique, virtually all significant positioning errors can be eliminated and the resulting differential positions can achieve superior accuracy. Limitations of early differential GPS technology included the cost, reliability and form factor of the systems.

Differential GPS was originally developed based on single-frequency receivers which used only the civilian signal. The first commercial dual frequency GPS system, which makes use of both the L1 frequency and the L2 frequency, was introduced in the mid 1980s. Using both signals allows for significant reductions in the time required to calculate a precise position and an increase in the working range of GPS devices.

Other technologies have been developed to address specific issues or applications. For example, in 1993 NovAtel introduced Narrow Correlator tracking technology which significantly reduced the effects of multipath interference which is caused by the reflection of multiple GPS signals. This innovation has allowed for a significant increase in accuracy. Comparable versions of this technology have been broadly adopted by the industry.

Another innovation was on-the-fly initialization which enabled differential GPS to be applied to receivers in motion while maintaining accuracy to within a few centimetres. This technology broadened the application of GPS to unmanned and automated vehicles.

NovAtel has introduced numerous additional technological innovations over the past ten years. See “Item 4 — Information on the Company, Business Overview — Technology.” These and other technological innovations have enabled the significant expansion of applications for high precision GPS positioning solutions.

### ***Continued Reduction in the Cost of Peripheral Component Technology***

High-precision GPS component suppliers, including the Company, as well as system integrators have benefited from significant reductions in the cost of peripheral components such as microprocessors, memory and wireless communications technology. These savings have enabled a significant reduction in the overall cost of GPS solutions and have driven an expansion in the number of applications using the technology. Management of the Company believes that this trend will continue to promote growth for the high precision segment of the GPS industry.

### ***Other Industry Trends***

In addition to the growth trends set forth above, management of the Company believes that growth of the high precision segment will be driven by the outsourcing of core GPS technology by OEMs and system integrators and the development of complementary technologies that will enhance the performance and functionality of existing GPS technology.

#### ***Outsourcing of Core GPS Technology by OEMs and System Integrators***

A number of NovAtel’s key competitors and OEM customers have historically developed core GPS technology in-house or have acquired stand alone GPS component vendors. Management of the Company believes there is

currently a trend among OEMs and system integrators to outsource core GPS technology to vendors such as NovAtel. By doing so, these companies are attempting to re-focus on their core competencies, developing custom systems for end market applications, which may enable them to make better use of their capital and other resources. Management of the Company also believes it is becoming increasingly difficult for these companies to provide cost effective and technically advanced precision GPS receivers relative to GPS focused companies, such as NovAtel, that have strong patent positions, substantial continuous GPS development and the ability to leverage their receiver technology across multiple applications and customers.

#### *Development of Complementary Technology*

Management of the Company believes that the development of complementary technology that enhances or augments the accuracy and reliability of the core GPS technology will enable a multitude of new applications for the technology and drive further growth. For example, the integration of inertial technology with GPS enables the combined system to provide full position and velocity information while the receiver passes through areas of signal blockage. There are a number of other complementary technologies that are expected to cause an acceleration in the number of applications using the technology.

#### **Barriers to Entry**

Management of the Company believes there are significant barriers to entry in the industry, including:

- proprietary and patented technology;
- scarcity of industry expertise; and
- extensive, established relationships with market leading customers and partners.

#### **Mission and Strategy**

NovAtel's goal is to become the leading provider of high-precision global positioning component technologies and sub-systems. In order to achieve this goal, NovAtel is focused on the following growth strategies:

- continue to invest in high-precision global positioning technology;
- partner with and/or acquire enabling and complementary technologies;
- continue to build market share with large OEMs and emerging system integrators;
- attract and retain key employees; and
- continue to generate strong revenue growth while improving profitability and capital efficiency.

#### *Continue to Invest in High-Precision Global Positioning Technology*

The Company is committed to continual improvement of the accuracy, reliability, cost and quality of its technology. To achieve these objectives, the Company intends to invest in research and development primarily in the following areas: (i) core GPS hardware and software; (ii) technology supporting the modernization of the GPS system; (iii) technology supporting other satellite based positioning systems; and (iv) technology that augments the Company's global positioning technology.

#### *Partner with and/or Acquire Enabling and Complementary Technologies*

NovAtel continually seeks to develop strategic partnerships with industry leaders of enabling and complementary technologies, such as inertial systems, guidance technology and wireless communications. The

Company also expects to continue to pursue selective strategic acquisitions that complement current product offerings, expand its market opportunity or broaden its customer base.

*Continue to Build Market Share with Large OEMs and Emerging System Integrators*

The Company plans to continue to build market share and enhance its growth through leveraging its OEM business model. Furthermore, the Company expects to continue to develop relationships with emerging system integrators through its growing international dealer network. An important element of this strategy is to continue to work with OEMs and system integrators in a highly collaborative fashion and to provide them with an exceptional level of customer support.

*Attract and Retain Key Employees*

NovAtel has assembled a talented and experienced team with proven expertise in the GPS industry. As the Company experiences growth, it intends to hire employees with demonstrated experience and ability, with the objective of increasing the number of highly productive teams. Potential employees are offered the opportunity to work for an industry leader on challenging assignments in their area of core competency with access to state-of-the-art development resources. The Company also maintains a competitive performance based compensation program which is designed to attract and retain employees.

*Continue to Generate Strong Revenue Growth while Improving Profitability and Capital Efficiency*

The Company intends to continue to pursue profitable growth opportunities through its focus on return on investment. Key elements of this strategy include: (i) maintaining selling prices and gross margins by pursuing value added high-precision global positioning applications; (ii) improving capital efficiency through outsourcing select business activities, manufacturing services and certain design functions; and (iii) investing in initiatives to improve efficiency and reduce costs while continuing to deliver superior customer service.

**Products**

NovAtel offers a broad range of high-precision GPS and other positioning components and sub-systems. The Company's products combine specialized hardware with proprietary software to enable its customers to fully integrate the Company's technology into their respective products and systems. NovAtel's products include GPS receivers, antennas, proprietary software and augmented GPS products.

A critical component of NovAtel's products are its GPS receivers which process the satellite signals received through the antenna to determine precise positions. A key advantage of NovAtel's GPS receivers is that they are highly flexible and configurable allowing the same receiver to be used across a broad range of applications. For example, NovAtel can install different software on the same type of receiver to meet the specific requirements of customers. This benefits NovAtel through reduced unit costs, higher production rates, focused research and development efforts and a streamlined product line. NovAtel's customers also benefit in that they are able to upgrade their systems on a cost-effective basis by installing new software as opposed to having to replace the entire receiver. NovAtel's GPS receivers are also capable of storing and running customer applications, enabling NovAtel's customers to realize cost-efficiencies and accelerated time to market.

NovAtel offers a range of antennas that are capable of supporting both single frequency and dual-frequency receivers and may be incorporated into a broad range of applications, including those which operate in dynamic or challenging environments.

NovAtel has also developed a range of proprietary high-precision GPS positioning software that, working in conjunction with its hardware, enables its customers to achieve accuracies to within a few centimetres, in real-time, while providing a high degree of reliability.

NovAtel leverages the components described above in its aviation and geomatics product lines as well as in its augmented GPS products, such as the SPAN product family. The SPAN product family integrates third-party inertial measurement technology with the Company's GPS technology (receiver, antenna and software) to provide the user with continuous positioning data even when a GPS signal has been temporarily lost.

NovAtel acquired Waypoint Consulting in 2005. This acquisition provided NovAtel with a new post-processing software product line which the Company believes is a leader in the photogrammetry market. One of the software products post-processes GPS and inertial measurements and fits directly into the SPAN product family mentioned above.

In September 2005, NovAtel also announced its next generation of GPS receivers ("OEMV") which include improved multipath elimination technology and optional GLONASS capability. The OEMV product family complies with the upcoming EU regulations governing the use of hazardous substances.

In addition, in 2005, the Company successfully developed a GPS/Galileo receiver, and has been selected as part of an industrial team to develop and supply the reference receivers for the Galileo monitoring and ground control system.

The following are the Company's most popular products with a brief explanation of their features and applications.

#### OEM4-G2



- High-performance dual-frequency engine for system integration
- Pulse Aperture Correlator (PAC™) tracking



- Our most popular GPS board
- Used in a multitude of applications from surveying to UAVs

#### ProPak-LBplus



- Includes L-band technology for autonomous decimeter-level accuracy
- Pulse Aperture Correlator (PAC™) tracking



- Ideal for real-time applications such as precision agriculture and GIS

#### GPS-700 Series



- Lightweight and featuring Pinwheel™ technology
- Eliminates the need for more expensive choke ring antennas



- Designed for any application requiring single or dual-frequency precise positioning

#### WAAS Reference Receiver G-II



- Superior Tracking and integrity verification of GPS and GEO satellites
- 50% improvement in performance of MEDLL multipath elimination



- Designed for use in WAAS, MSAS, GAGAN and EGNOS air traffic control ground infrastructure systems

#### SMART ANTENNA



- Self-contained GPS receiver and antenna
- 12-channel parallel all-in-view tracking of L1 C/A code and carrier phase



- Rugged housing suitable for marine and precise timing applications
- Used in precision agriculture

## SUPERSTAR II



- Compact size with low power consumption
- Carrier phase capable
- Standard SBAS support



- Ideal for precision timing, marine applications, or asset tracking
- Easy integration for meter-level performance

## OEMV Family



- Single, dual and tri-frequency configurations
- Optional L1/L2 GLONASS
- Integrated L-band
- Vision Correlator Technology



- Increased ability to work in difficult environments with combined GPS and GLONASS capabilities

## Markets

Management of the Company believes there are three primary drivers of future growth in the high-precision global positioning industry:

- increased sales into existing applications in traditional markets;
- development of new applications in non-traditional markets; and
- development of new applications in emerging markets.

### *Increased Sales into Existing Applications in Traditional Markets*

Management of the Company believes sales of existing applications will continue to increase in markets that have been traditional users of GPS technology. Generally, these are markets where GPS has either replaced older technology, such as the marine industry, or markets where GPS technology was adopted at an early stage largely because the benefits of GPS outweighed price sensitivity, such as the survey and mapping market.

The Company expects these markets to continue to expand for a number of reasons including:

- continued reductions in the price of GPS technology are expected to make existing applications more cost-effective for a broader range of users;
- development of new technology is expected to enhance the functionality of existing applications; and
- outsourcing of core GPS technology by OEMs and system integrators is expected to increase.

Selected examples of growth applications in traditional markets include surveying and mapping, aviation and air traffic navigation ground infrastructure and commercial marine.

### *Development of New Applications in Non-Traditional Markets*

New applications continue to emerge within established markets that to date have not been traditional users of GPS technology. The growth in new applications is largely being driven by OEMs and system integrators who are developing new products that have become commercially viable as a result of technological improvements, cost reductions and the development of complementary technology.

Selected examples of growth applications in non-traditional markets include precision agriculture and mining and construction machine control.



## *Development of New Applications in Emerging Markets*

New applications are also being developed within markets that have been created or transformed as a result of the evolution of low-cost, high-precision positioning technology. These markets represent a diverse range of significant growth opportunities for the Company.

Selected examples of applications in emerging markets include unmanned air vehicles, airborne weapons training and precision asset tracking and guidance.

### **Customers**

NovAtel competes in the high-precision global positioning market by selling components and sub-systems to leading OEMs and system integrators in multiple industries. During the past two years NovAtel has sold its products to over 400 customers worldwide, including some of the leading companies in their respective sectors.

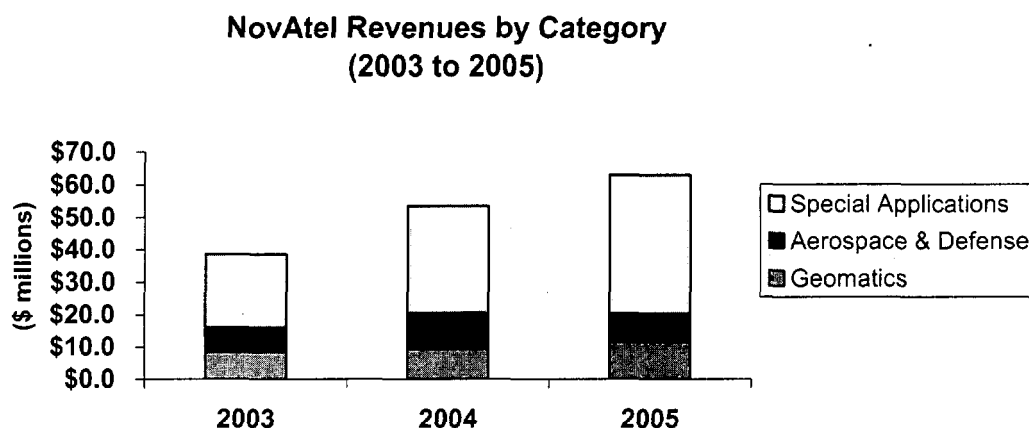
For the fiscal year ended December 31, 2005, NovAtel's 10 largest customers represented 64% of revenue.

Sales to key customers, Leica Geosystems, Beijing BDStar, and Raytheon Systems, accounted for 18%, 11%, and 6%, respectively, of the Company's total revenues in 2005. In comparison, sales to Leica Geosystems, Beijing BDStar, and Raytheon Systems accounted for 16%, 8%, and 15%, respectively, of the Company's total revenues in 2004. See "Item 4 — Information on the Company, Business Overview — Strategic Partnerships — Leica Geosystems" and "Item 3 — Key Information, Risk Factors — Dependence on Key Customers."

The Company's proportionate share of sales by Point accounted for 9% of total revenues in 2005 compared to 11% of total revenues in 2004.

In 2005, the Company derived 41% of its revenues in the United States, 21% in Asia/Australia, 28% in Europe, 7% in Canada and 3% in other parts of the world.

The Company divides its customers into three primary market categories, Special Applications, Geomatics and Aerospace and Defence. The following chart sets out the consolidated revenues of the Company by the categories indicated for the fiscal years ended December 31, 2003, 2004 and 2005.



### ***Special Applications***

Special Applications is the largest and fastest growing category, contributing \$42.6 million or 67% of NovAtel's revenues for the fiscal year ended December 31, 2005. This category has experienced a 37% compounded annual growth rate from 2002 to 2005. This group's customers are in diverse markets, including precision agriculture, marine, mining and machine control, unmanned vehicles and sports media.

Special Applications has three main types of customers:

- large, industry leading companies utilizing NovAtel's proprietary solutions to develop replacement and transformative products for their end-markets, such as Leica Geosystems in the survey market or AGCO in precision agriculture;
- innovative system integrators that have developed new markets through creative integration of NovAtel's products with other technology, such as BEELINE; and
- dealers and distributors that service hundreds of smaller companies that are developing innovative solutions for existing and new markets.

NovAtel's dealers and distributors are critical in extending the market reach of the Company. In many cases, these organizations make the first sales to small system integrators that grow to become significant customers through the development of innovative product offerings. This was the case for Beijing BDStar, which is now one of NovAtel's largest customers.

### ***Geomatics***

Geomatics (surveying and mapping) was one of the first commercial applications of high-precision GPS technology and is currently a well-established market. The Geomatics category contributed \$11.5 million, or 18%, of NovAtel's revenues for the fiscal year ended December 31, 2005. Revenue in NovAtel's Geomatics category consists primarily of sales attributable to Point, the Company's joint venture with Sokkia. Point provides Sokkia's global marketing organization with advanced measurement solutions for the fields of surveying, mapping, geographic information systems, construction and construction machine control. Sokkia's distribution system includes more than 25 subsidiaries and representatives around the world, each having its own dealer network. The geomatics category also includes revenues from third party customers which comprised approximately 23% of the geomatics category in 2005. NovAtel's sales to Leica Geosystems, although primarily for geomatics applications, are not included in this category for reporting purposes due to historical classification.

Given the relative maturity of this market, growth in the sale of traditional GPS products is expected to be moderate. However, management of the Company believes that GPS modernization and the introduction of the Galileo system represent significant opportunities for future growth as end-users upgrade their equipment in order to realize the enhanced performance and efficiencies that may be achieved through the utilization of the new signals.

### ***Aerospace and Defence***

Aerospace and defence continue to be strong markets for GPS technology and include some of the most technically demanding applications of NovAtel's products. The Aerospace and Defence category contributed \$8.9 million or 14% of NovAtel's revenues for the fiscal year ended December 31, 2005. Customers of the Company in this group utilize NovAtel's high-precision positioning technology for critical components in such applications as the ground networks of civil air traffic navigation systems, and in-flight guidance systems on board aircraft that together enable aircraft to determine their precise position, and certain military applications.

The Company's family of Wide Area Augmentation System ("WAAS") receivers is a key component of revenue in this category. The WAAS receivers are an important part of the existing ground infrastructure that supports the next generation of air traffic navigation systems for commercial aviation in North America, Europe, Japan, China and India. Raytheon Company, the Federal Aviation Administration ("FAA") and other leading companies and national aviation organizations around the world have selected NovAtel as a key receiver and signal generator supplier for this application primarily because of NovAtel's leading technology in this area.

Management of the Company believes that opportunities for future growth within the aviation and defence markets will be driven by such developments as the introduction of the Galileo system and the use of commercial

grade receivers in defence applications such as unmanned vehicles. The Company has successfully developed GPS/Galileo receivers, and has been selected as part of an industrial team to develop and supply the reference receivers for the Galileo monitoring and ground control system.

The Company is currently working with OEMs and system integrators that have determined precision GPS technology can be utilized in many military applications such as training, logistics and missile tracking which do not require the use of encrypted military GPS technology.

### **Sales, Marketing and Distribution**

NovAtel sells, markets and distributes its products through both direct and indirect channels in order to maximize market coverage on a cost-effective basis. The primary focus for NovAtel's sales and marketing efforts is on OEM customers, strategic relationships and supporting a network of dealers and resellers. The Company has developed its sales and marketing capabilities in anticipation of and in response to customer needs as they arise in its multiple markets. The in-house sales and marketing efforts are focused on market research, product management, customer service, distribution management, communications and promotions. Each market receives specific attention to the needs of its sales and distribution channels, which are rapidly changing.

The Company believes that providing a high level of customer technical support is critical to creating and maintaining strong relationships with their OEM and system integrator customers. The Company is able to achieve this level of support by employing a sufficient number of qualified engineers and technicians to advise and provide customers with integration and after-sale support. Due to frequent interaction with customers, these integration engineers and support technicians also act as an important source of customer information, which can drive product enhancements, new product ideas and new business opportunities.

### **Technology**

NovAtel has invested significant funds and resources to become a leading provider of high-precision positioning technology. Since 1992, NovAtel has provided several major technological innovations to meet the increasingly demanding needs of the high-precision positioning industry. NovAtel currently holds 30 U.S. patents and various related foreign patents in jurisdictions such as Canada, Europe and Japan which expire at various dates no earlier than November 28, 2010 and has numerous pending U.S. and foreign patent applications. Some of the more significant technology developments by the Company are discussed below.

#### *1992 Narrow Correlator Tracking Technology*

NovAtel established itself in the GPS industry through the introduction of its patented Narrow Correlator tracking technology in 1992. Narrow Correlator tracking allowed NovAtel products to provide positioning accuracy to within one meter with a single-frequency receiver while significantly reducing the effects of multipath interference caused by the reflection of multiple GPS signals. Relative to other GPS technology available at the time, this innovation resulted in a five-fold improvement in accuracy for GPS devices.

#### *1994 Multipath Elimination Technology ("MET")*

NovAtel continued its technology advancements with the introduction of MET in 1994. MET expanded upon the Narrow Correlator tracking technology by refining software algorithms to more effectively filter the effects of multipath signal interference. This new technology removed 25% to 50% of the residual multipath errors.

#### *1995 Multipath Estimating Delay Lock Loop ("MEDLL")*

In 1995, NovAtel introduced MEDLL technology. MEDLL offered a more rigorous approach to the reduction of multipath effects using improved circuitry, software control and processing. The MEDLL technology further reduced the effects of multipath interference by up to 90%.

### *1995 Real Time Kinematic ("RTK") Signal Processing Technology*

Also in 1995, NovAtel introduced a unique method of applying RTK processing to the carrier frequency signals in order to rapidly increase the accuracy of the computed position from meters to less than 20 centimeters. This signal processing method is particularly useful for single frequency GPS receivers. Previous attempts at using RTK resulted in significant delays before reaching precision accuracies.

### *2000 Pinwheel™ Aperture Coupled Slot Array Technology*

In 2000, NovAtel introduced a new antenna utilizing its patented Pinwheel™ Aperture Coupled Slot Array technology. Using this technology, the Company was able to produce a much smaller and lighter antenna than other available antennas on the market without sacrificing either accuracy or reliability.

### *2000 Pulse Aperture Correlation ("PAC") Technology™*

Also in 2000, NovAtel introduced its new PAC™ technology. Available exclusively on the Company's OEM4 product line, PAC™ technology implements the latest digital signal processing techniques to provide superior tracking capability in the presence of multipath interference. PAC effectively doubles the accuracy of the Narrow Correlator tracking technology and reduces interference by up to eight times.

### *2002 Model Position Aiding and Position Velocity Filter*

In 2002, NovAtel developed a method of increasing the reliability of GPS position output in very challenging environments through the use of model position aiding and position velocity filter techniques. While this technology was initially developed to meet the needs of a specific application, Management of the Company believes that it can be applied to a broader range of markets, such as precision agriculture.

### *2003 GPS and Micro-Electro-Mechanical System ("MEMS") Integration*

In 2003, the Company developed software that enables the integration of its GPS receivers with a MEMS system. This system can maintain an accurate estimate of position and velocity without the use of GPS satellite signals for short periods of time. In the absence of GPS satellite signals, a GPS receiver cannot provide information about the user's position or velocity if the direct line-of-sight between the receiver and the satellites is blocked. The integration of GPS and MEMS allows the combined system to provide full position and velocity information while the receiver passes through areas of signal blockage.

### *2004 GPS Modernization and Integration of Inertial Navigation Systems ("INS")*

In 2004, the Company developed equipment designed to generate and receive the new GPS L5 civil signal. In support of the Company's air traffic navigation ground infrastructure business, the new L5 equipment will generate the signal used by WAAS Ground Uplink Stations and will also control and monitor the quality of the signal produced by the WAAS geostationary satellites.

The Company continued its technology advancement in the area of integrating GPS and INS technologies, resulting in two patents.

### *2005 Vision Correlator and Vision Products, GLONASS and Galileo*

In 2005, the Company acquired the exclusive rights to the multipath mitigation technique ("MMT") from the Communication Sciences Corporation for applications in commercial non-military markets. The Company invested in the commercialization of this technology, resulting in design changes within its GPS Digital Signal Processing and software processing sections. The Company's brand name for this new technology is Vision Correlator. The

Vision Correlator is embedded in the Company's latest OEMV family of products and will provide a significant improvement in detecting and removing the harmful effects of multipath signal interference, upon release.

The Company's OEMV family of products also includes optional GLONASS capability. In addition, in 2005, the Company successfully developed GPS/Galileo receivers, and has been selected as part of an industrial team to develop and supply the reference receivers for the Galileo monitoring and ground control system.

## **Research and Development**

The Company's technology position is supported by a strong commitment to research and development. NovAtel has invested heavily in developing GPS technology, including the design of proprietary software and integrated circuits for GPS receivers. The Company's research and development expense, net of customer funded programs, was \$10.9 million, \$9.6 million and \$7.1 million in 2005, 2004 and 2003, respectively.

In addition, the Company also receives significant amounts of funding from its customers through NRE contracts to conduct research and development on their behalf. Typically, NovAtel retains ownership of the intellectual property developed under these arrangements and is able to exploit such intellectual property for its own purposes. The Company's total engineering expenditures comprised of internal research and development programs and customer funded programs, were \$15.4 million or 24% of revenue in 2005, \$13.1 million or 24% of revenue in 2004, and \$10.6 million or 28% of revenue in 2003.

Often a new product is initially developed for a customer or strategic partner who is willing to purchase development stage products. The Company has used feedback from such initial customers as a source of information in designing and refining its products, and in defining, with greater precision, customer needs in emerging market areas.

## **Competition**

NovAtel faces competition primarily from other developers and suppliers of high-precision positioning component technology which is sold to OEMs and system integrators for commercial applications, as well as from OEMs who choose to develop and produce the component technology in-house.

The primary competitors supplying component technology to OEMs and system integrators vary by each industry or market served, but generally include Trimble Navigation Limited (U.S.), Thales Group (France), Topcon Positioning Systems (Japan), Javad Navigation Systems (U.S.), NavComm Technologies (U.S.) and at the single-frequency level, companies such as CSI Wireless Inc. (Canada) and Furuno Marine Electronics (Japan). While these competitors to NovAtel offer high-precision positioning solutions to OEMs, many also develop, produce and market products that are sold directly to end-users and are therefore in competition with the OEMs' end-products and solutions.

NovAtel works with OEMs in a highly collaborative and cooperative process to provide them with the core technology that becomes integrated into their end products and solutions. Management of the Company believes that the non-competitive nature of its relationships with OEMs is a key differentiator and a competitive advantage for the Company relative to other suppliers.

## **Strategic Partnerships**

### ***Leica Geosystems***

The Company entered into a strategic co-operation agreement with Leica Geosystems on May 1, 2003, to jointly develop new technology for GPS in the high-precision geomatics market. The initial term of the agreement is seven years. Under the terms of the agreement, NovAtel has agreed to develop custom versions of existing GPS receivers and other components for Leica Geosystems. In September 2003, pursuant to the strategic co-operation

agreement, the Company entered into a supply agreement with Leica Geosystems which sets forth the arrangements under which NovAtel would develop and supply Leica Geosystems with a custom GPS receiver. In February 2004 and February 2005, Leica Geosystems announced the launch of new products that incorporate NovAtel's GPS receiver and antenna technology. In October 2005, Leica Geosystems was acquired by Hexagon AB of Sweden. The Company does not expect this transaction to affect its business with Leica Geosystems. In addition, the Company, Leica Geosystems and CMC Electronics entered into a change of control agreement dated April 5, 2004, which provides Leica Geosystems with certain rights in the event of the acquisition of control of NovAtel by certain competitors of Leica Geosystems. See "— Certain Contractual Rights" and "Item 3 — Key Information, Risk Factors — Dependence on Key Customers."

#### ***Point, a NovAtel/Sokkia Joint Venture***

The Company owns 49% of the common shares in Point, a geomatics joint venture with Sokkia, one of the world's largest suppliers of surveying and mapping equipment. The Company sells GPS receivers and antennas to Point which incorporates these products into surveying systems that are in turn sold through the Sokkia distribution channels and through independent dealers and distributors. In addition, the Company provides facilities, computer support and development and logistical support for Point's Calgary operations. See "Item 3 — Key Information, Risk Factors — Dependence on Key Customers."

#### ***CMC Electronics***

The Company and CMC Electronics entered into a strategic co-operation agreement on April 5, 2004, to cooperate in the development of new technology for GPS aviation solutions and under which the Company would develop and supply global positioning products and technology to CMC Electronics. CMC Electronics is one of the world's largest suppliers of certified GPS products into the commercial aviation market. The initial term of the agreement is ten years. Under the terms of the agreement, for so long as the Company is CMC Electronics' sole and exclusive supplier of global positioning products and technologies for certain specified avionics markets and ground based augmentation systems, NovAtel has agreed not to sell such products and technology for use in such markets. In consideration for agreeing to such restrictions, the Company is entitled to receive minimum payments of \$2.4 million in the initial four year period of the agreement. NovAtel's revenue with CMC Electronics in 2005 was approximately \$1.1 million, or 1.7% of total revenue. See "Item 3 — Key Information, Risk Factors — Dependence on Key Customers."

#### **Certain Contractual Rights**

Pursuant to the terms of a strategic co-operation agreement dated April 5, 2004, Leica Geosystems has the unilateral right in the case where a defined competitor of Leica Geosystems obtains (1) 50% of the voting shares of the Company, (2) the power to elect a majority of the Board of Directors, or (3) obtain a significant portion of the Company's technology, to cancel the strategic co-operation agreement and any related development and supply agreements signed between the Company and Leica Geosystems, the right to purchase the intellectual property developed by the Company on behalf of Leica Geosystems (while providing the Company a license to use such intellectual property in its ongoing business) and in the event of a material disruption in supply to deal directly with the Company's suppliers (subject to appropriate compensation to the Company).

#### **Employees**

A key priority of the Company is to attract, train and retain talented employees. NovAtel views its highly skilled and performance-motivated employees as a competitive advantage and a key part of the strategy for future growth. The Company staff turnover rate was approximately 10% for its fiscal year ending December 31, 2005 (excluding Point employees and involuntary separations).

As at December 31, 2003, 2004 and 2005, the Company (excluding Point) had the following full-time employees:

<u>Department</u>	<u>Full-Time Employees</u>		
	<u>2003</u>	<u>2004</u>	<u>2005</u>
Research and development .....	67	75	84
Operations .....	32	37	52
Administration and finance .....	21	22	23
Sales and marketing .....	18	16	21
TOTAL .....	<u>138</u>	<u>150</u>	<u>180</u>

The Company also retained six part-time, five temporary employees and one contract personnel as at December 31, 2005. Separately, Point employed 44 permanent employees and one temporary employee as at December 31, 2005. None of NovAtel's employees are represented by a labour union, and the Company has not experienced any work stoppages.

### **Operations and Facilities**

NovAtel's registered and head office is located in Calgary, Alberta. The Company's office space totals approximately 46,000 square feet and is subject to a ten-year lease that expires in 2009, with an option for NovAtel to extend the term for a further five-year period. In December 2004, the Company exercised an option under the lease that requires the owner of the Calgary facility to build an expansion of approximately 22,000 square feet. The expansion is expected to be ready for occupancy in July 2006. At this location, the Company assembles, tests, packages and ships most of NovAtel's products including GPS receivers and antennas.

The circuit card assemblies, which are a primary component of NovAtel's GPS receiver, are manufactured by contract suppliers in accordance with NovAtel design, manufacturing and testing requirements. NovAtel has two primary subcontract suppliers of circuit card assemblies.

### **Patents, Trademarks and Licenses**

NovAtel currently holds 30 U.S. patents and various related foreign patents in jurisdictions such as Canada, Europe and Japan which expire at various dates no earlier than November 28, 2010, and has numerous pending U.S. and foreign patent applications. The Company also currently has numerous trademarks worldwide, including the NovAtel trademark, which is registered or pending in 31 countries. See "Item 3 — Key Information, Risk Factors — Patents and Proprietary Rights; Patent Litigation."

NovAtel has copyrights and intellectual property rights to its proprietary software and custom integrated circuit designs. In 1997, the Company purchased a license with respect to its SoftSurv software, which is a full-featured GPS dual frequency data post-processing package software for surveying applications. In 1999, NovAtel licensed SoftSurv and certain intellectual property related to end user products to Point. See "Item 4 — Information on the Company, Business Overview — Strategic Partnerships — Sokkia/Point Joint Venture."

The Company acquired the exclusive rights to the multipath mitigation technique ("MMT") from the Communication Sciences Corporation for applications in commercial non-military markets. The Company invested in the commercialization of this technology, resulting in design changes within its GPS Digital Signal Processing and software processing sections. The Company's brand name for this new technology is Vision Correlator. The Vision Correlator is embedded in the Company's latest OEMV family of products and provides a significant improvement in detecting and removing the harmful effects of multipath signal interference

### **Legal Proceedings**

In November 1994, the Company commenced an action against Trimble Navigation Limited ("Trimble") seeking relief and damages for an alleged infringement of the Company's U.S. Patent No. 5,101,416 (the "Narrow Correlator patent"). In March 1995, Trimble commenced an action against the Company seeking relief and damages

for an alleged infringement of Trimble's U.S. Patent No. 5,390,207 (the "207 patent"). In January 1996, Trimble filed a complaint with the International Trade Commission in the U.S. seeking to ban imports of the Company's products into the U.S. which allegedly infringed upon the 207 patent. All of these claims were resolved on July 16, 1996 when the Company and Trimble entered into a settlement agreement by cross licensing certain technologies, including a Narrow Correlator license to Trimble. The 1996 settlement agreement with Trimble includes a provision that Trimble may, at its sole option, terminate the licenses and rights granted upon a direct change of control. As of December 31, 2005, intangible assets of the Company included \$77,000 related to the settlement agreement with Trimble. On June 26, 2001, NovAtel received notice from Trimble terminating the licenses and rights under the settlement agreement in connection with the share acquisition of the Company by CMC Electronics in April 1998. The Company has sought legal advice regarding Trimble's termination rights under the 1996 settlement agreement and continues to evaluate the impact, if any, of Trimble's notice of termination. As of the date hereof, the Company has not provided for any impairment of these intangible assets in its financial statements. The Company does not expect this issue to materially affect the financial position, results of operations, or liquidity of the Company.

Other than the foregoing, there are no outstanding legal proceedings material to the Company that the Company is aware of to which the Company, its subsidiaries or any of its properties are subject, nor are there any such proceedings known to be contemplated.

### **C. Organizational Structure**

On April 17, 1998, CMC Electronics purchased approximately 58% of the Company's total shares outstanding from the Company's two principal shareholders. From January 2005 to August, 2005, CMC Electronics sold approximately 4.5 million common shares of NovAtel through open market transactions, reducing its ownership of the Company from approximately 55% to nil%.

The Company does not have any significant subsidiaries.

### **D. Property, Plant and Equipment**

See "Item 4 — Information on the Company, Business Overview — Operations and Facilities."

## **Item 4A. Unresolved Staff Comments**

None.

## **Item 5. Operating and Financial Review and Prospects**

### **A. Operating Results**

*Management's discussion and analysis is a review of the results of operations and the liquidity and capital resources of the Company. It should be read in conjunction with the selected financial data and the consolidated financial statements of the Company and the notes thereto included elsewhere in this Annual Report. Certain information included herein is forward looking and based upon assumptions and anticipated results that are subject to uncertainties. Should one or more of these uncertainties materialize or should the underlying assumptions prove incorrect, actual results may vary significantly from those expected. See "Item 3 — Key Information, Risk Factors."*

*The Company prepares its financial statements in Canadian dollars and in conformity with Canadian generally accepted accounting principles ("Canadian GAAP"). The Company is required to reconcile the material differences between Canadian GAAP and U.S. generally accepted accounting principles ("U.S. GAAP"). Such reconciliation is set forth in Note 23 of the consolidated financial statements of the Company included elsewhere in this Annual Report.*

### **Executive Overview**

NovAtel designs, markets and sells high-precision GPS and other positioning component technology and sub-systems for a wide variety of commercial applications principally in the aviation, geomatics (surveying and mapping), mining, precision agriculture, marine and defence industries. NovAtel's solutions combine hardware,



such as receivers and antennas, with software to enable its customers to fully integrate the Company's high-precision GPS technology into their respective products and systems. Unless the context requires otherwise, references herein to "NovAtel" or the "Company" refer to NovAtel Inc., including its interest in its joint venture, Point.

The Company's goal is to become the leading provider of high precision GPS component technology and subsystems. In order to achieve this objective, NovAtel's management focuses on achieving average long-run organic revenue growth of 15% to 20% per year (prior to currency fluctuations). Since the Company's top ten customers generated 64% of revenue in 2005, NovAtel's ability to achieve its revenue projections and revenue growth will be largely dependent on maintaining successful relationships with its key customers and strategic partners, as well as forming relationships with new key OEM customers.

A substantial portion of the Company's operating costs are relatively fixed in the short-term, and consequently, NovAtel's short-term profitability is largely dependent on achieving projected revenues and forecasted gross margins as a percentage of revenue.

In order for the Company to maintain its technology position within its market, the Company's management believes that continued significant investment in research and product development programs is required and expects research and development costs, net of customer funding, will be 16% to 19% of revenue in the near term.

As part of the Company's growth strategy, the Company also focuses on managing working capital, particularly inventory and trade accounts receivable.

The Company uses performance based incentive programs for both senior management and employees. Incentive pay under these programs is dependent on the Company achieving certain corporate objectives, such as operating income targets.

Most of the Company's revenues (over 95% in 2005) are earned in currencies other than the Canadian dollar, principally the U.S. dollar. A substantial portion of the Company's expenses, however, have been and will continue to be incurred in Canadian dollars. Accordingly, fluctuations in exchange rates between the U.S. dollar and the Canadian dollar could materially affect results of operations.

The Company's results of operations have fluctuated and can be expected to continue to fluctuate on a periodic basis as a result of a number of factors which affect revenue, gross margin and operating expenses. Annual and quarterly revenues have fluctuated because of a number of factors, including acquisition of new product lines, timing of major contracts, U.S. dollar to Canadian dollar exchange rates, operating results of subsidiary and joint venture entities, certification and market acceptance of the Company's new products, impact and timing of large orders, pricing pressures in the market, establishing and maintaining effective distribution channels, fluctuations in non-recurring engineering ("NRE") fees, seasonality of customer purchase patterns and the timing of industry trade shows.

NovAtel's consolidated financial statements include a 49% proportionate share of the accounts of Point, a geomatics joint venture with Sokkia, as required under Canadian GAAP. The Company sells products to Point which incorporates them into surveying systems that are in turn sold through the Sokkia distribution channels and through independent dealers and distributors. In addition, the Company provides facilities, computer support and development and logistical support for Point's Calgary operations. The Company's consolidated Statements of Operations include the proportionate share of each of the equivalent line items reflected on Point's Statement of Operations. Similarly, the Company consolidates its proportionate share of each line item of Point's balance sheet.

On May 14, 2003, the Company acquired CMC Electronics' non-aviation L1 GPS OEM product line. The new product line extended the Company's current high-performance, upgradeable L1 and L1/L2 product line into the mid-level L1 market. This increased the Company's total addressable market in core sectors and also created entry points into new vertical markets, such as timing and marine. The purchase price was comprised of \$150,000 at closing and \$600,000 payable over time as a royalty on the revenue generated by this product line. NovAtel expects the \$600,000

royalty payment will be paid out in full by the end of 2006. CMC Electronics' non-aviation L1 GPS OEM product line contributed approximately \$3.4 million in revenue in 2005 compared to \$4.4 million in 2004.

On October 1, 2005, the Company acquired Waypoint Consulting Inc. ("Waypoint") for approximately \$3.5 million in cash, subject to post closing adjustments to working capital. Of the total purchase price, \$2.2 million was paid by December 31, 2005 and \$1.2 million held in escrow will be paid in installments over three years, subject to certain conditions. Waypoint's products include specialized real-time and post-processing GPS and /inertial positioning and trajectory software. The Company plans to leverage Waypoint's products, intellectual property and expertise across a number of market applications.

## **Revenue and Expenses**

Revenues include product sales and NRE fees. NRE fees are received by the Company from its customers under engineering service contracts. Revenues from product sales consist primarily of sales of OEM receivers, software upgrades, GPS antennas, WAAS type receivers and end user products primarily for the survey and mapping market. The Company classifies its revenues into the following three primary categories, Geomatics, Aerospace and Defence, and Special Applications.

The Geomatics category is made up of surveying and mapping markets. Geomatics revenues are largely comprised of NovAtel's sales to Point, net of intercompany eliminations, and NovAtel's 49% proportionate share of sales by Point.

The Aerospace and Defence category is made up of aviation and defence markets. These markets utilize the Company's precision positioning technology for critical components in civil air traffic navigation, flight management systems, and certain military applications.

The Special Applications category is made up of marine, precision agriculture, unmanned vehicles, construction/grading, dealers (other than those that can be identified with a particular market sector) and miscellaneous markets.

The Company typically maintains control of the technology developed under NRE contracts allowing it to use these technologies to improve its current products and develop new products and solutions.

Total revenue has increased year over year since 2001 at a compounded annual growth rate of 22% through sales to new customers as well as through sales of additional products and services to existing customers.

Cost of product sales consists primarily of the cost of the raw materials and components, labour, manufacturing overhead and provisions for obsolete inventory and provisions for warranty obligations. Cost of NRE fees consists primarily of personnel and related costs incurred in providing the engineering services.

Gross margin as a percentage of revenue varies primarily as a result of product sales mix, changes in materials and contract manufacturing costs, liquidation of discontinued inventory and absorption of fixed manufacturing costs.

Research and development expenses consist primarily of compensation and benefit costs of engineering personnel, contracted research and development expenses, amortization of purchased technology, amortization of equipment costs, and facility and computer support costs. Research and development expenses are reduced to the extent they are funded under customer contracts and other engineering development contracts.

Selling and marketing expenses consist primarily of compensation and benefit costs of sales and marketing personnel as well as expenses for advertising, promotion and trade shows, dealer and agent's commissions, facilities and other expenses related to the sale of products.

General and administration expenses consist primarily of compensation and benefit costs of administrative personnel, professional fees such as legal, audit and insurance costs, corporate overhead, computer support costs and facilities expenses.

## Critical Accounting Estimates

The Company applies a number of critical accounting estimates in preparing the consolidated financial statements. A discussion of the Company's critical accounting estimates follows.

### *Revenue Recognition*

The Company recognizes product revenue when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable and collectibility is reasonably assured. Revenues from non-recurring engineering fees are recognized at the time services are rendered. On long-term contracts, in which the customer pays established rates for time and materials, revenue is recognized as services are rendered and costs are incurred. On certain long-term contracts, revenue is recognized using the proportional performance method relative to customer milestones achieved. Revisions in cost and profit estimates during the course of work are reflected in the period in which the need for revision becomes known. Losses, if any, are recognized fully when first anticipated. Some contracts contain penalty provisions based on performance relative to established targets. Such penalties are included in revenue or cost estimates when amounts can be reasonably determined.

In 2005, approximately \$4.0 million, or 6.3%, of the Company's revenue was derived from NRE fees. Approximately 35% of these revenues were recognized from contracts on which the customer paid established rates for time and materials and 65% were recognized from contracts that contained customer milestones.

The Company applies U.S. Statement of Position 97-2, *Software Revenue Recognition*, to product sales where software is considered more than incidental. For software arrangements involving multiple elements, the Company allocates revenue to each element based on the relative fair value or the residual method, as applicable, and using vendor specific objective evidence of fair values, which is based on prices charged when the element is sold separately. Software revenue is recognized when persuasive evidence of an arrangement exists, the software is delivered in accordance with all terms and conditions of the customer contracts, the fee is fixed or determinable and collection is reasonably assured. Revenue related to post-contract support ("PCS"), including technical support and unspecified when-and-if available software upgrades, is recognized ratably over the PCS term.

As of December 31, 2005, the Company had deferred revenue of \$184,000 in accordance with its software revenue recognition policies.

At the time the Company recognizes revenue, the Company reduces the measurement of revenue by an estimate of the expected product returns and price adjustments. The provision for product returns and price adjustments is assessed for adequacy at each quarter-end and is based on recent historical experience and known customer claims. The provision for product returns and price adjustments was \$281,000 as of December 31, 2005 compared to \$262,000 at December 31, 2004, with the increase attributable to an increase in revenue.

Effective with the fourth quarter of 2002, the Company changed its policy of recognizing revenue on shipments of product from the Company to Point from revenue recognition at the time of shipment to revenue recognition at the time of receiving payment from Point, due to the uncertainty of collecting payment on the associated receivables. As of December 31, 2005, the Company had deferred revenue related to product shipments to Point of \$555,000, net of inter-company eliminations. The Company would revert to its prior policy of recognizing revenue at the time of shipment if the Company is able to determine that reasonable assurance of collecting payment from Point exists. This determination would be based on Point's ability to demonstrate sustained improved operating performance and/or Point receiving additional financial support from the Company and Sokkia sufficient to enable Point to meet its financial obligations on an ongoing basis.

### *Inventories*

Raw materials and components, work-in-progress, and finished goods inventories are recorded at the lower of cost and net realizable value. Cost is determined on a first-in, first-out basis and includes materials, labour and manufacturing overhead.

The Company establishes provisions for obsolete or excess inventory. The Company's products have product life cycles that range on average from two to four years. At both the product introduction and product discontinuation stage, there is a higher degree of risk of inventory obsolescence. In 2005, the provision for obsolete and excess inventory included in the statement of operations was \$147,000 or 0.2% of revenue, compared to \$450,000 or 0.8% of revenue in 2004, with the lower provision in 2005 related to the Company's improved procedures for managing its inventories.

The estimate of the provision for obsolete and excess inventory is partially based on expected future product sales, which are difficult to forecast for certain products. As of December 31, 2005, the Company had approximately \$600,000 (gross value before inventory provisions) of first generation WAAS and older generation GPS receiver inventory for which no firm customer commitments were on hand. Based on the Company's assessment of future market opportunities, the Company expects that the value of this inventory will not be realized through future sales, and, accordingly, has established provisions to reduce the net value of this inventory to \$nil. As at December 31, 2005, the provision for obsolete and excess inventory was \$1.5 million or 22% of the gross value of inventory, compared to \$2.0 million or 28% at December 31, 2004, with the decrease caused by disposal of certain obsolete inventory items in 2005.

#### ***Allowance for Doubtful Accounts***

The Company establishes provisions for doubtful accounts receivable. These provisions are established at the time revenue is recognized and are re-evaluated at each quarter end for adequacy. In determining the adequacy of the provision, the Company considers known uncollectable or at-risk receivables as well as the aging profile of other receivables. In 2005, the provision for doubtful accounts included in the statement of operations was \$20,000 or 0.03% of revenue, compared to \$179,000 or 0.3% of revenue in 2004, with the lower provision in 2005 attributable to a decrease in the amount of uncollectable receivables from customers.

As at December 31, 2005, the provision for doubtful accounts was \$799,000 or 6.8% of the gross value of the third party receivables compared to \$945,000 or 8.9% at December 31, 2004. The lower dollar amount of the provision reflects a write-off of certain older uncollectible customer receivables in 2005.

#### ***Provision for Future Warranty Costs***

Warranty costs are accrued, to the extent that they are not recoverable from third party manufacturers, for the estimated cost to repair products for the balance of the warranty periods.

The Company's products are covered by standard warranty plans that extend normally 12 months to 18 months from the date of product shipment. Certain customers negotiate warranty terms that range up to three years.

The Company provides for the costs of expected future warranty claims at the time of product shipment. The adequacy of the provision is assessed at each quarter end and is based on historical experience of warranty claims and costs. As of December 31, 2005, the Company's provision for future warranty claims was \$693,000 compared to \$538,000 as of December 31, 2004, with the increase attributable primarily to increased revenue from product shipments.

#### ***Research and Development Costs and Deferred Development Costs***

Research costs are charged to operations as incurred. Development costs, including software development costs, are charged to operations as incurred unless they meet specific criteria related to technical, market and financial feasibility. In these circumstances, the costs are deferred and amortized on a systematic basis, subject to an estimate of recoverability.

In 2005, the Company deferred development costs of \$nil related to the development of a certified aviation GPS receiver, compared to \$218,000 in 2004. With the GPS receiver having reached the commercialization stage, the Company amortizes these deferred costs, using a method similar to the unit-of-production method of amortization. The Company amortized \$538,000 of these deferred costs in 2005 compared to \$416,000 in 2004.

At December 31, 2005 the Company had deferred \$1.7 million of development costs (\$2.4 million at December 31, 2004). The continued deferral of these costs is subject to recoverability based on estimates of future sales of the certified aviation GPS receiver. On April 5, 2004, the Company and CMC Electronics entered into a Strategic Cooperation Agreement which *inter alia* provides for certain guaranteed future payments over the following four years. Under the current business programs between the Company and CMC Electronics, the Company would expect these future payments to substantially recover the \$1.7 million of deferred development costs as of December 31, 2005. Should future actual sales of this receiver be materially lower than the current estimated sales, all or a portion of the deferred development costs would be charged to results of operations. The Company assesses the recoverability of the deferred development costs at each quarter end.

### ***Income Taxes***

The Company follows the liability method of accounting for income taxes. Under this method, current income taxes are recognized for the estimated income taxes payable for the current year. Future income tax assets and liabilities are recognized for temporary differences between the tax and accounting bases of assets and liabilities as well as for the benefit of losses available to be carried forward to future years for tax purposes that are more likely than not to be realized.

As of December 31, 2005, the Company had income tax benefits related to previously incurred income tax losses, research and development costs, depreciation deductible for tax purposes and investment tax credits totaling approximately \$140 million, which are available to reduce future taxable income and taxes payable, primarily for Canadian purposes.

Prior to 2004, the Company had established a full valuation allowance against the calculated tax benefits, since it was uncertain that these tax benefits were more likely than not to be realized. In determining the valuation allowances to establish against these deferred tax benefits, the Company considers many factors, including the specific taxing jurisdiction, the carry forward period, income tax strategies, limitations due to acquisitions-of-control and forecasted earnings. A valuation allowance is recognized if, based on the weight of available evidence, the Company concludes that it is more likely than not that some portion or all of the deferred tax benefits will not be realized. Effective 2004, and continuing in 2005, the Company determined, on the basis of consecutive years of increasing profitability from 2001 to 2005 and the Company's forecasts of operating results for the foreseeable future, that it was more likely than not that a portion of the future income tax assets would be realized. As part of this analysis, the Company used a seven year moving average of forecasted profitability for its operations subject to Canadian income tax.

Accordingly, the Company recognized future income tax assets of \$5.6 million on its balance sheet as of December 31, 2005, and a corresponding \$2.4 million future income tax benefit in its statement of operations for the year ended December 31, 2005. In 2004, the Company recognized \$3.2 million of future income tax assets on its balance sheet as of December 31, 2004, and a corresponding \$1.1 million future income tax benefit and \$2.1 million benefit of investment tax credits in its statement of operations for the year ended December 31, 2004.

As of December 31, 2005, the valuation allowance against the calculated future income tax assets was approximately \$44.2 million, or 89% of the gross value of the future income tax assets.

If the Company's forecasted profitability in the foreseeable future were 20% above or 20% below current estimates, the future income tax benefit included in the statement of operations for the year ended December 31, 2005, would have been approximately \$3.5 million and \$1.3 million, respectively.

## Results of Operations

The following table sets out, as a percentage of revenue, consolidated operations data for the periods indicated.

	Year Ended December 31,		
	2005	2004	2003
	(Percentage of Revenue)		
Revenues .....	100.0%	100.0%	100.0%
Gross profit — product sales .....	62.4	59.9	53.9
Gross profit — NRE fees .....	42.0	43.1	45.5
Total gross profit .....	61.1	58.3	52.5
Operating expenses:			
Research and development .....	17.2	17.8	18.4
Selling and marketing .....	10.1	10.7	13.6
General and administration .....	11.2	9.8	11.1
Foreign exchange loss .....	0.4	1.1	1.3
Share offering costs .....	—	1.4	—
Total operating expenses .....	38.9	40.8	44.4
Operating income .....	22.2	17.5	8.1
Interest income, net .....	1.2	0.5	0.4
Other expense .....	(0.1)	(0.1)	(0.4)
Benefit of investment tax credits .....	2.5	8.1	—
Income from continuing operations before income taxes .....	25.8	26.0	8.1
Income taxes			
Current provision .....	3.2	4.3	0.1
Future income tax expense (benefit) .....	(3.8)	(2.0)	—
Total income tax expense (benefit) .....	(0.6)	2.3	0.1
Net income from continuing operations .....	26.4	23.7	8.0
Income (loss) from discontinued operations .....	—	0.1	0.9
Net income .....	26.4%	23.8%	8.9%

### 2005 Compared to 2004

#### Revenues

Total revenues in 2005 were \$63.3 million, representing a 17% increase over 2004 revenues of \$53.9 million, despite the adverse impact of the weaker U.S. dollar relative to the Canadian dollar. Since the majority of the Company's revenues are denominated in U.S. dollars, a weaker U.S. dollar adversely affects NovAtel's revenues. NovAtel's U.S. dollar denominated revenue declined to an average of \$1.22 Canadian in 2005 from an average of \$1.30 Canadian in 2004. If the Company's U.S. dollar denominated revenues were converted into Canadian dollars at equivalent exchange rates, revenue in 2005 would have been approximately 25% higher than in 2004.

The following table sets out revenues of the Company by the market categories indicated for the fiscal years ended December 31, 2005 and 2004.

	2005		2004		Change	
	\$	%	\$	%	\$	%
	(\$000's)					
Geomatics .....	\$11,534	18%	\$ 9,339	17%	\$ 2,195	24%
Aerospace and Defence .....	8,883	14	11,248	21	(2,365)	(21)
Special Applications .....	42,596	67	32,952	61	9,644	29
Other .....	282	—	393	1	(111)	(28)
<b>TOTAL .....</b>	<b>\$63,295</b>	<b>100%</b>	<b>\$53,932</b>	<b>100%</b>	<b>\$ 9,363</b>	<b>17%</b>

#### *Geomatics*

In 2005, approximately 77% of Geomatics revenues were comprised of NovAtel's sales to Point, net of intercompany eliminations and the Company's proportionate share of sales by Point. The balance of geomatics revenue was derived from sales to third party customers. Geomatics sales were \$11.5 million in 2005, an increase of 24% from \$9.3 million in 2004, due primarily to higher sales to third party customers in Canada and Asia, as well as higher NRE revenue associated with new product development for Point.

Point's operations were restructured in April 2002, with the aim of focusing operating activities on sales, marketing and distribution as opposed to product development. NovAtel had been disappointed in the operating performance of Point, particularly the lower than expected revenues which the Company anticipated would increase after the April 2002 restructuring. The Company continues to work with Point's management and Sokkia to improve the operating results of Point.

#### *Aerospace and Defence*

Aerospace and Defence revenues were \$8.9 million in 2005 compared to \$11.2 million for 2004, a decrease of 21%. The Company's Aerospace and Defence revenues are highly dependent on the timing of large, government-funded programs. The majority of the revenue in 2005 related to the U.S. WAAS and Indian GAGAN aviation programs that contributed \$4.1 million in revenue in 2005 compared to \$8.2 million in 2004. The lower revenue was anticipated and was attributable to the substantial completion of major phases of three WAAS related contracts in 2004. In the latter half of 2005, the Company also recognized initial revenue of \$1.1 million under a contract funded by the European Space Agency ("ESA") to develop the Ground Reference Receiver for the European Galileo program.

The certified GPS receiver jointly developed by the Company and CMC Electronics is intended for use in airborne applications and the local area augmentation system ("LAAS") program. With the GPS receiver achieving certification, the Company earned royalties of \$800,000 in 2005, compared to \$545,000 in 2004.

In October 2004, the Canadian Space Agency (CSA) awarded a contract to the Company for demonstration and prototype receiver development for the European Galileo system. The value of CSA's contribution to NovAtel under the contract is \$997,000, of which \$595,000 was recognized as revenue in 2005. This contract is expected to be completed in the first half of 2006.

In November 2005, the Company commenced work on the Galileo Safety of Life project under a CSA contract with CMC Electronics. The Company expects to receive \$500,000 funding on this program over approximately 18 months, with equipment deliveries scheduled for May 2007.

In 2005, the Company received a contract for a portion of the Galileo Reception Chain (GRC) reference receiver development as part of the European Galileo program. The initial contract valued at Euro 1.3 million, will run from June 2005 to mid 2006. Should the contract proceed to a full award, the program may have a value up to Euro 6.3 million over the next two and a half years with delivery of up to 25 production receivers subsystems by mid 2008. The Company recognized \$1.1 million in revenue in 2005 under this contract.

### *Special Applications*

Special Applications revenues were \$42.6 million in 2005 compared to \$33.0 million in 2004, an increase of 29%. The increase was primarily attributable to higher product shipments to Leica Geosystems of \$2.6 million, higher shipments of product into China of \$2.6 million and higher shipments to the Company's U.S. dealer network of \$2.8 million.

The Company entered into a strategic co-operation agreement with Leica Geosystems in May 2003 to jointly develop new technology for GPS in the high-precision geomatics market. In September 2003, pursuant to the strategic co-operation agreement, NovAtel also entered into a supply agreement with Leica Geosystems which sets forth the arrangements under which NovAtel would develop and supply a custom GPS receiver for Leica Geosystems. In 2004 and 2005, Leica Geosystems announced the launch of new survey products that incorporate NovAtel's GPS receiver and antenna technology. The Company's revenue with Leica Geosystems accounted for 18% of total revenue in 2005 and the Company expects revenue from product shipments supplied to Leica Geosystems to comprise between 15% and 20% of NovAtel's total revenue in 2006.

### *Revenues by Geographic Market*

In 2005, the Company derived approximately 52% of its total revenues from the sale of products to countries outside the United States and Canada compared to 48% in 2004. Revenues from such international sales increased to \$33.2 million in 2005 from \$25.8 million in 2004, primarily as a result of higher shipments to Leica Geosystems and into China.

### *Gross Profit*

Gross profit increased to \$38.7 million in 2005 from \$31.4 million in 2004, mainly as a result of increased revenue. Gross profit as a percentage of total revenues increased to 61.1% in 2005 from 58.3% in 2004. The increase in gross margin as a percentage of revenue is primarily attributable to favourable product mix, including the benefit of Waypoint related products which are primarily software, a lower proportion of NRE fee revenues relative to product sales, and lower provisions for inventory obsolescence.

### *Research and Development*

Research and development expenses increased 14% from \$9.6 million in 2004 to \$10.9 million in 2005 but decreased as a percentage of total revenues from 17.8% in 2004 to 17.2% in 2005. The increase in research and development expenses is primarily attributable to higher material costs of \$523,000, higher employee compensation and benefit costs of \$343,000, higher costs for facilities and IT support services of \$378,000 and higher consulting and other outside service of \$298,000, partially offset by higher recovery of expenses from customer funded programs of \$418,000. The Company believes that significant investments in research and development are required to maintain its technology and compete in its business. The Company expects to spend approximately 17% to 19% of revenue in research and development activities in 2006.

### *Selling and Marketing*

Selling and marketing expenses increased 11% from \$5.8 million in 2004 to \$6.4 million in 2005 but decreased as a percentage of revenue from 10.7% in 2004 to 10.1% in 2005. The increased selling and marketing costs were due primarily to higher employee compensation and benefit costs of \$477,000, higher advertising and product promotion costs of \$307,000, partially offset by lower provision for doubtful customer accounts receivable of \$160,000. The Company expects to spend approximately 10% to 11% of revenue in selling and marketing activities in 2006.



## *General and Administration*

General and administration expenses increased 33% from \$5.3 million in 2004 to \$7.1 million in 2005 and increased as a percentage of revenue from 9.8% in 2004 to 11.2% in 2005. The increase in general and administration expenses was a result of higher professional fees for legal and audit services of \$667,000, higher employee compensation and benefit costs of \$460,000, higher insurance costs of \$441,000, higher amortization costs of \$170,000, higher board of director fees of \$100,000, and higher consulting costs related to the Company's Sarbanes-Oxley 404 compliance project of \$260,000, partially offset by higher allocations for facility and IT support to manufacturing, research and development and sales and marketing departments of \$550,000. The Company expects to spend approximately 9.5% to 10.5% of revenue in general and administration activities in 2006.

## *Foreign exchange loss*

Foreign exchange loss decreased from \$595,000 in 2004 to \$255,000 in 2005 due to a slowdown in the weakening of the U.S. dollar relative to the Canadian dollar.

## *Interest Income, net*

NovAtel earned net interest income of \$787,000 in 2005 compared to \$313,000 in 2004 as a result of higher cash balances available for investment and higher interest rates. The Company's cash deposits which are not required for operations are invested in short-term interest bearing instruments.

## *Benefit of Investment Tax Credits*

In 2005, the Company recognized a \$1.6 million benefit of investment tax credits related to the use of investment tax credits to shelter tax otherwise payable in 2005. In 2004, the Company recognized a \$4.4 million benefit of investment tax credits of which \$2.3 million was related to the use of investment tax credits to shelter tax otherwise payable in 2004 and \$2.1 million was related to the recognition of future income tax assets.

## *Provision for Current Income Taxes and Future Income Tax Benefit*

The provision for current income taxes consists primarily of an expense related to the benefit of investment tax credits recognized elsewhere on the statement of operations, a provision for income tax payable in the U.S., a provision for income tax payable in Canada related to Waypoint's operations prior to being amalgamated with the Company, and Canadian federal large corporations tax. The provision for current income taxes was \$2.0 million in 2005, compared to \$2.3 million in 2004. The decrease was mainly attributable to a lower expense incurred with the recognition of the benefit of investment tax credits.

In 2005, the Company recognized \$2.4 million future income tax benefit (see "Critical Accounting Estimates") compared to \$1.1 million in 2004. The Company recognized the future income tax benefit in 2005 on the basis of its improving profitability from 2001 to 2005 and the Company's forecasted profitability in the foreseeable future.

## *2004 Compared to 2003*

### *Revenues*

Total revenues in 2004 were \$53.9 million, representing a 39% increase over 2003 revenues of \$38.7 million, despite the adverse impact of the weaker U.S. dollar relative to the Canadian dollar. Since the majority of the Company's revenues are denominated in U.S. dollars, a weaker U.S. dollar adversely affects NovAtel's revenues. NovAtel's U.S. dollar denominated revenue declined to an average of \$1.30 Canadian in 2004 from an average of \$1.40 Canadian in 2003. If the Company's U.S. dollar denominated revenues were converted into Canadian dollars at equivalent exchange rates, revenue in 2004 would have been approximately 50% higher than in 2003.

The following table sets out revenues of the Company by the market categories indicated for the fiscal years ended December 31, 2004 and 2003.

	2004		2003		Change	
	\$	%	\$	%	\$	%
	(\$000's)					
Geomatics .....	\$ 9,339	17%	\$ 8,380	22%	\$ 959	11%
Aerospace and Defence .....	11,248	21	7,558	20	3,690	49
Special Applications .....	32,952	61	22,563	58	10,389	46
Other .....	393	1	183	—	210	>100
TOTAL .....	<u>\$53,932</u>	<u>100%</u>	<u>\$38,684</u>	<u>100%</u>	<u>\$15,248</u>	<u>39%</u>

#### *Geomatics*

In 2004, Geomatics revenues were largely comprised of NovAtel's sales to Point, net of intercompany eliminations and the Company's proportionate share of sales by Point. Geomatics sales were \$9.3 million in 2004, an increase of 11% from \$8.4 million in 2003, due primarily to higher sales volumes from the Company to Point, including NRE revenue associated with new product development.

#### *Aerospace and Defence*

Aerospace and Defence revenues were \$11.2 million in 2004 compared to \$7.6 million for 2003, an increase of 49%. The majority of the revenue in 2004 related to three U.S. WAAS aviation programs that contributed \$8.2 million in revenue, including \$5.2 million of hardware deliveries, in 2004 compared to \$4.7 million in 2003.

In early 2004, the Company completed a contract awarded by the FAA in 2002 to develop the next generation WAAS receiver. The Company received a letter subcontract from Raytheon Company for production start-up and 83 initial receiver deliveries, all of which were delivered in 2004. The contract has subsequently been amended to add another 22 WAAS receivers for delivery in early 2005. At the end of 2004, the contract had a combined NRE and production value of approximately U.S. \$3.7 million. The Company's NRE work under the program was substantially complete by the end of 2004.

NovAtel also participated in the new Geostationary Command & Control Segment program to develop Ground Uplink System receivers for the new third Geostationary Satellite for WAAS. In 2003, NovAtel received a letter subcontract from Raytheon worth up to U.S. \$1.64 million NRE plus U.S. \$885,000 in hardware deliverables. The Company's NRE work under the program was substantially complete by the end of 2004 and all hardware deliveries were completed.

In 2003, NovAtel received a letter subcontract from Raytheon Company for the development of an L1/L5 Signal Generator to be used with the new WAAS/GEO Ground Uplink System. This letter contract was worth up to U.S. \$1.0 million NRE plus U.S. \$592,000 in hardware deliverables. The Company's NRE work under the program was substantially complete by the end of 2004 and all hardware deliveries were completed.

#### *Special Applications*

Special Applications revenues were \$33.0 million in 2004 compared to \$22.6 million in 2003, an increase of 46%. The increase was primarily attributable to higher product shipments to Leica Geosystems of \$6.3 million, an increase in revenue from the GPS OEM L1 product line acquired in May 2003 from CMC Electronics of \$2.1 million, and higher shipments of product into China of \$2.4 million. The increase in Special Applications revenue was achieved despite the impact of the weaker U.S. dollar on revenues of the Company.

### *Revenues by Geographic Market*

In 2004, the Company derived approximately 48% of its total revenues from the sale of products to countries outside the United States and Canada compared to 43% in 2003. Revenues from such international sales increased to \$25.8 million in 2004 from \$16.5 million in 2003, primarily as a result of higher shipments to Leica Geosystems.

### *Gross Profit*

Gross profit increased to \$31.4 million in 2004 from \$20.3 million in 2003, mainly as a result of increased revenue. Gross profit as a percentage of total revenues increased to 58.3% in 2004 from 52.5% in 2003. The increase in gross margin as a percentage of revenue is primarily attributable to favourable product mix, including the benefit of aviation hardware shipments and a lower proportion of NRE fee revenues relative to product sales, and lower per unit manufacturing costs of the Company's GPS receivers.

### *Research and Development*

Research and development expenses increased 35% to \$9.6 million in 2004 from \$7.1 million in 2003 but decreased as a percentage of total revenues to 17.8% in 2004 from 18.4% in 2003. The increase in research and development dollars reflects higher employee compensation and benefit costs of \$2.2 million, including higher provisions for employee incentive programs, higher amortization costs of \$183,000 relating to equipment and higher non-related party consulting costs of \$273,000. In addition, in 2003, the Company incurred one time costs of \$441,000 related to the acquisition of CMC Electronics' non-aviation L1 GPS OEM product line.

### *Selling and Marketing*

Selling and marketing expenses increased 9.1% to \$5.8 million in 2004 from \$5.3 million in 2003 but decreased as a percentage of total revenues to 10.7% in 2004 from 13.6% in 2003. The increased selling and marketing costs were primarily due to higher employee compensation and benefit costs, including higher provisions for employee incentive programs of \$600,000, higher employee relocation costs of \$50,000, higher travel costs of \$83,000, partially offset by lower distribution costs in Asia of \$160,000, and lower provision for doubtful customer accounts receivable of \$192,000.

### *General and Administration*

General and administration expenses increased 24.1% to \$5.3 million in 2004 from \$4.3 million in 2003 but decreased as a percentage of total revenues to 9.8% in 2004 from 11.1% in 2003. The increased expenses are attributable to higher employee compensation and benefit costs including higher provisions for employee incentive programs of \$767,000, employee relocation expenses of \$42,000 and increased professional fees of \$260,000.

### *Share Offering Costs*

In 2004, the Company incurred \$754,000 of expenses related to a proposed public offering in Canada and a private placement in the U.S. of its common shares. On May 26, 2004, the Company withdrew the offering. As the Company did not proceed with the offering, the Company has expensed the \$754,000 within the Consolidated Statements of Operations for the year ended December 31, 2004.

### *Interest Income, net*

NovAtel earned net interest income of \$313,000 in 2004 compared to \$174,000 in 2003 as a result of higher cash balances available for investment. The Company's cash deposits which are not required for operations are invested in short-term interest bearing instruments.

### *Other Expense*

Other expense in 2004 was \$67,000 compared to \$137,000 in 2003 and consisted primarily of cash discount costs related to early payment on sales to Sokkia by Point in both years.

### *Benefit of Investment Tax Credits*

In 2004, the Company recognized a \$4.4 million benefit of investment tax credits, of which \$2.3 million was related to the use of investment tax credits to shelter tax otherwise payable in 2004 and \$2.1 million was related to the recognized future income tax asset. There was no comparable benefit of investment tax credits in 2003, as the Company used tax losses to shelter tax otherwise payable and had not had a sufficient record of profitability to recognize the future benefit.

### *Provision for Current Income Taxes and Future Income Tax Benefit*

The provision for current income taxes consists primarily of an expense related to and equal to the benefit of investment tax credits recognized elsewhere on the statement of operations and Canadian federal large corporations tax. The provision for current income taxes was \$2.3 million in 2004, compared to \$52,000 in 2003. The increase was mainly attributable to an expense incurred with the recognition of the benefit of investment tax credits and a higher tax base for Canadian federal large corporations tax.

In 2004, the Company recognized \$1.1 million future income tax benefit (see "Critical Accounting Estimates") compared to \$nil in 2003. The Company recognized the future income tax benefit in 2004 on the basis of its improving profitability from 2001 to 2004 and the Company's forecasted profitability in the foreseeable future.

### *Income (Loss) from Discontinued Operations*

In 2004, the Company recognized income from discontinued operations of \$21,000 compared to \$360,000 in 2003, attributable to the liquidation of the residual assets and liabilities of its former subsidiary, Mezure, which was discontinued in 2003.

## Quarterly Results of Operations

The following tables set out certain financial information for each of the eight quarters ended December 31, 2005. In the opinion of management of the Company, this information has been prepared on the same basis as the audited financial statements appearing elsewhere in this Annual Report, and all necessary adjustments have been included in the amounts stated below to fairly present the unaudited quarterly results when read in conjunction with the Company's audited financial statements and the notes to those statements. The operating results for any quarter should not be relied upon as any indication of results for any future period.

	Quarter Ended							
	2005				2004			
	Dec. 31	Sept. 30	Jun. 30	Mar. 31	Dec. 31	Oct. 2	Jun. 30	Mar. 31
Revenue .....	\$16,157	\$14,295	\$17,486	\$15,357	\$14,371	\$13,777	\$13,282	\$12,502
Cost of sales .....	5,905	5,614	6,817	6,300	6,201	5,409	5,330	5,563
Gross profit .....	10,252	8,681	10,669	9,057	8,170	8,368	7,952	6,939
Operating expenses:								
Research and development .....	3,056	2,606	2,882	2,338	2,758	2,394	2,398	2,038
Selling and marketing ....	1,480	1,689	1,651	1,567	1,218	1,485	1,594	1,454
General and administration .....	1,928	1,520	1,817	1,817	1,377	1,325	1,304	1,306
Foreign exchange loss (gain) .....	19	196	32	8	320	325	(72)	22
Share offering costs .....	—	—	—	—	12	20	722	—
Total operating expenses ..	6,483	6,011	6,382	5,730	5,685	5,549	5,946	4,820
Operating income .....	3,769	2,670	4,287	3,327	2,485	2,819	2,006	2,119
Interest income, net .....	246	218	170	153	118	87	55	53
Other income (expense) ....	(12)	(16)	(30)	(14)	(15)	(17)	(16)	(19)
Benefit of investment tax credits .....	556	—	—	1,036	4,356	—	—	—
Income from continuing operations before income taxes .....	4,559	2,872	4,427	4,502	6,944	2,889	2,045	2,153
Income taxes								
Current provision .....	549	75	109	1,313	2,276	18	22	12
Future income tax expense (benefit) .....	(1,121)	(371)	(355)	(555)	(1,091)	—	—	—
Total income tax expense (benefit) .....	(572)	(296)	(246)	758	1,185	18	22	12
Net income from continuing operations ....	\$ 5,131	\$ 3,168	\$ 4,673	\$ 3,744	\$ 5,759	\$ 2,871	\$ 2,023	\$ 2,141

	Quarter Ended							
	2005				2004			
	Dec. 31	Sept. 30	Jun. 30	Mar. 31	Dec. 31	Oct. 2	Jun. 30	Mar. 31
	(Percentage of Revenues)							
Revenues .....	100%	100%	100%	100%	100.0%	100.0%	100.0%	100.0%
Gross profit .....	63.4	60.7	61.0	59.0%	56.9	60.7	59.9	55.5
Operating expenses:								
Research and development .....	18.9	18.2	16.5	15.2	19.2	17.4	18.1	16.3
Selling and marketing ....	9.2	11.8	9.4	10.2	8.5	10.8	12.0	11.6
General and administration .....	11.9	10.6	10.4	11.8	9.6	9.6	9.8	10.5
Foreign exchange loss (gain) .....	0.1	1.4	0.2	0.1	2.2	2.3	(0.5)	0.2
Share offering costs .....	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>	<u>0.0</u>	<u>0.1</u>	<u>0.1</u>	<u>5.4</u>	<u>—</u>
Total operating expenses ..	<u>40.1</u>	<u>42.0</u>	<u>36.5</u>	<u>37.3</u>	<u>39.6</u>	<u>40.2</u>	<u>44.8</u>	<u>38.6</u>
Operating income .....	23.3	18.7	24.5	21.7	17.3	20.5	15.1	16.9
Interest income, net .....	1.6	1.5	1.0	1.0	0.8	0.6	0.4	0.4
Other income (expense) ....	(0.1)	(0.1)	(0.2)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)
Benefit of investment tax credits .....	<u>3.4</u>	<u>0.0</u>	<u>0.0</u>	<u>6.7</u>	<u>30.3</u>	<u>—</u>	<u>—</u>	<u>—</u>
Income from continuing operations before income taxes .....	28.2	20.1	25.3	29.3	48.3	21.0	15.4	17.2
Income taxes								
Current provision .....	3.4	0.5	0.6	8.5	15.8	0.2	0.2	0.1
Future income tax expense (benefit) .....	<u>(7.0)</u>	<u>(2.6)</u>	<u>(2.0)</u>	<u>(3.6)</u>	<u>(7.6)</u>	<u>—</u>	<u>—</u>	<u>—</u>
Total income tax expense (benefit) .....	<u>(3.6)</u>	<u>(2.1)</u>	<u>(1.4)</u>	<u>4.9</u>	<u>8.2</u>	<u>0.2</u>	<u>0.2</u>	<u>0.1</u>
Net income from continuing operations ....	<u>31.8%</u>	<u>22.2%</u>	<u>26.7%</u>	<u>24.4%</u>	<u>40.1%</u>	<u>20.8%</u>	<u>15.2%</u>	<u>17.1%</u>

The following table sets out revenues of the Company by the market categories indicated for the last eight fiscal quarters.

	Quarter Ended							
	2005				2004			
	Dec. 31	Sept. 30	Jun. 30	Mar. 31	Dec. 31	Oct. 2	Jun. 30	Mar. 31
	(\$000's)							
Geomatics .....	\$ 2,339	\$ 3,010	\$ 3,719	\$ 2,466	\$ 2,803	\$ 2,273	\$ 2,171	\$ 2,092
Aerospace and Defence ....	2,988	1,326	2,901	1,668	2,141	3,515	3,457	2,135
Special Applications .....	10,783	9,874	10,841	11,098	9,211	7,906	7,647	8,188
Other .....	<u>47</u>	<u>85</u>	<u>25</u>	<u>125</u>	<u>216</u>	<u>83</u>	<u>7</u>	<u>87</u>
TOTAL .....	<u>\$16,157</u>	<u>\$14,295</u>	<u>\$17,486</u>	<u>\$15,357</u>	<u>\$14,371</u>	<u>\$13,777</u>	<u>\$13,282</u>	<u>\$12,502</u>

The Company's quarterly results of operations have fluctuated and are expected to continue to fluctuate because of a number of factors which affect revenue, gross margins and operating expenses, including revenue generated from major contracts, acquisition of new product lines, U.S. dollar to Canadian dollar exchange rates, operating results of joint venture and subsidiary entities, new product introductions, fluctuations in NRE fees, seasonality and other factors affecting customer purchase patterns, and the timing of industry trade shows.

In addition, revenues can be expected to vary significantly as a result of a lack of a significant order backlog, fluctuations in demand for existing products, the rate of development of new markets, the degree of market

acceptance of new products, increased competition and the general strength of domestic and international economic conditions. Furthermore, if the Company were unable to deliver sufficient quantities of products in a timely manner, due to factors such as parts supply shortages or customs delays, its revenues could be adversely affected.

In 2005, quarterly operating expenses fluctuated due to the impact of changes in staffing levels, recovery of research and development expenses from NRE fees, legal fees, and provisions related to the Company's employee incentive programs and senior management bonus program.

### **Liquidity and Capital Resources**

In 2005, cash provided by operations was \$17.1 million, compared to \$12.5 million in 2004. Cash provided by operations in 2005 consisted primarily of \$16.7 million of net income and \$2.9 million in amortization expenses, partially offset by the effect of a \$2.4 million non-cash future income tax benefit and a \$1.0 million increase in working capital. The increase in working capital was caused mainly by an increase in accounts receivable, partially offset by an increase in accounts payable and accrued liabilities.

Cash provided by financing activities in 2005 was \$778,000, consisting of \$721,000 related to the exercise of employee stock options and reimbursement of \$57,000 from CMC Electronics, Inc. relating to the proposed public offering/private placement of the Company's shares in 2004. In 2004, \$598,000 in cash was provided by financing activities, \$1.5 million of which was also related to employee stock option exercises, partially offset by expenses related to the proposed public offering/private placement of the Company's shares of \$807,000 and capital lease payments of \$100,000.

Cash used in investing activities in 2005 was \$24.1 million, consisting of purchases of \$56.4 million of short-term investments, partially offset by proceeds from maturities of short-term investments of \$38.4 million, \$3.5 million related to the acquisition of Waypoint, \$2.4 million of capital equipment and \$221,000 in royalty payments made to CMC Electronics in connection with the purchase of its former OEM GPS business. In 2004, cash used in investing activities was \$6.6 million, consisting of purchases of \$17.7 million of short-term investments, partially offset by proceeds from maturities of short-term investments of \$13.9 million, purchases of \$2.3 million of capital equipment, capitalized expenditures of \$218,000 related to the development of a certified GPS aviation receiver, and \$261,000 royalty payments made to CMC Electronics, also in connection with the purchase of its former OEM GPS business.

At December 31, 2005, NovAtel had cash and short-term investments of \$35.1 million. The Company has credit agreements with HSBC Bank Canada and The Toronto Dominion Bank under which it can borrow up to \$1.7 million for day-to-day operating requirements and \$3.4 million to support the margin requirement related to the purchase of up to approximately U.S. \$14.0 to \$15.0 million of foreign exchange contracts (depending on the maturity date of the contracts). The lines of credit are payable on demand and are secured by certain of the Company's assets. At December 31, 2005, portions of the lines of credit were utilized to support approximately U.S. \$8.5 million of foreign exchange contracts (U.S. \$7.5 million at December 31, 2004), leaving \$1.7 million available for day-to-day operating requirements and the margin capacity necessary to enter into additional U.S. \$5.5 to \$6.5 million in forward exchange contracts (depending on the maturity date of the contracts).

The Company believes that its existing cash, cash equivalents, short term investments, available lines of credit and anticipated cash generated from operations will be sufficient to satisfy its currently anticipated cash needs for at least the next twelve months.

### **Taxes**

The Company's operations are substantially located in Canada and accordingly, Canada is the Company's main tax jurisdiction. The Company has not recorded a provision for current income taxes payable in Canada, other than for Canadian federal large corporations tax, income tax related to Waypoint's operations prior to amalgamation with NovAtel, due to previously incurred losses, credits and costs. As of December 31, 2005, the Company had

approximately \$140 million of losses, investment tax credits, depreciation and research and development costs that are available to reduce future taxable income and taxes payable primarily in Canada. The Company has determined that the acquisition of a majority of its Common Shares by CMC Electronics in 1998, BAE SYSTEMS p.l.c.'s acquisition of the majority of the common shares of CMC Electronics in November 1999, and ONCAP's acquisition of the majority of the common shares of CMC Electronics in April 2001 each constitute an acquisition of control of the Company for Canadian income tax purposes. Accordingly, the availability of certain of the Company's Canadian income tax losses, research and development costs, depreciation deductible for tax purposes and investment tax credit may be subject to limitation. The ultimate availability and amount of these losses, credits and costs may be dependent upon future Canada Revenue Agency audits.

Prior to 2004, the Company had established a full valuation allowance against the calculated tax benefits associated with tax shields, since it was uncertain that these tax benefits were more likely than not to be realized. In determining the valuation allowances to establish against these deferred tax benefits, the Company considers many factors, including the specific taxing jurisdiction, the carry forward period, income tax strategies, limitations due to acquisitions-of-control and forecasted earnings. A valuation allowance is recognized if, based on the weight of available evidence, the Company concludes that it is more likely than not that some portion or all of the future tax benefits will not be realized. In 2004 and 2005, the Company determined, on the basis of consecutive years of increasing profitability from 2001 to 2005 and the Company's forecasts of operating results for the foreseeable future, that it was more likely than not that a portion of the future income tax assets would be realized. As part of this analysis, the Company used a seven year moving average to forecast profitability of its operations subject to Canadian income tax.

Accordingly, the Company recognized future income tax assets of \$5.6 million (\$2.4 million current and \$3.2 million long term) on its balance sheet as of December 31, 2005, and a corresponding \$2.4 million future income tax benefit in its statement of operations for the year ended December 31, 2005.

## **Outlook**

Management of the Company expects revenues to increase as a result of the addition of new customers, the sale of additional products and services to existing customers, the acquisition of Waypoint on October 1, 2005, as well as through the implementation of the Company's overall growth strategy. NovAtel's management expects to achieve average long-run organic revenue growth of 15% to 20% per year, prior to currency fluctuations.

The Company's U.S. dollar denominated revenue generated an average of \$1.22 Canadian dollar per U.S. dollar in 2005. As of May 4, 2006, the U.S. dollar was valued at approximately \$1.11 per Canadian dollar. The Company currently expects that product shipments to Leica Geosystems will represent 18% to 22% of 2006 revenues. The acquisition of Waypoint is expected to contribute approximately \$2.3 million revenue in 2006 compared to approximately \$500,000 in 2005. The Company expects gross profit generated on product sales and NRE fees to increase in conjunction with the expected increase in revenue. Research and development expenses are expected to increase to support evolving technological needs and new product development. Sales and marketing expenses and general and administrative expenses are also anticipated to increase to support the anticipated growth in the Company's business.

In addition, the Company expects to incur general and administrative expenses in 2006 of approximately \$1.0 million as part of its Sarbanes-Oxley Section 404 program compared to approximately \$500,000 in 2005.

## **Off Balance Sheet Arrangements**

As of December 31, 2005, the Company had no off balance sheet arrangements other than operating leases. The Company has a commitment to fund approximately \$1.4 million related to leasehold improvements with respect to an expansion of its Calgary facility.



## Contractual Obligations

The following table sets forth the Company's contractual obligations and commitments to make future payments under contracts, excluding trade and related party trade payables.

	Payments Due by Period				
	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 years
			(\$000's)		
Capital lease obligations .....	\$ —	\$ —	\$ —	\$ —	\$ —
Operating leases .....	14,685	1,078	2,505	2,636	8,466
Purchase obligations for inventory, capital assets and services .....	11,518	11,503	15	—	—
Notes payable .....	<u>1,552</u>	<u>1,552</u>	—	—	—
<b>TOTAL .....</b>	<b><u>\$27,755</u></b>	<b><u>\$14,133</u></b>	<b><u>\$2,520</u></b>	<b><u>\$2,636</u></b>	<b><u>\$8,466</u></b>

## Related Party Transactions

On May 14, 2003, the Company acquired CMC Electronics' non-aviation L1 GPS OEM product line. The purchase price was comprised of \$150,000 at closing and \$600,000 payable over time as a royalty on the revenue generated by this product line. To date, the Company has paid \$564,000 of royalty payments to CMC Electronics. The Company expects the remaining \$36,000 royalty payment will be paid by the end of Q1 2006. The transaction was reviewed and approved by a committee of independent directors of the board of directors of the Company.

During the first quarter of 2005, the Company sold \$124,000 of products to CMC Electronics, and charged \$241,000 in royalties related to the development of a certified aviation GPS receiver. CMC Electronics charged the Company \$10,000 equipment service charges in Q1 2005. From January 2005 through August 2005, CMC Electronics sold its interest in NovAtel, does not maintain any representation on the Company's board of directors and therefore is not considered to be a related party, effective May 11, 2005.

The Company and CMC Electronics entered into a strategic co-operation agreement on April 5, 2004, to jointly develop new technology for GPS aviation solutions. The initial term of the agreement is ten years. Under the terms of the agreement, NovAtel has agreed to develop and supply global positioning products and technology to CMC Electronics. In addition, NovAtel has agreed to restrictions on its ability to sell its global positioning products and technology to certain specified markets, in consideration for the payment of certain minimum royalty payments. The transaction was reviewed and approved by a committee of independent directors of the board of directors of the Company.

In 2005, the Company sold \$4.4 million of products to Point, its joint venture with Sokkia. In addition, the Company provided \$300,000 in facilities, computer systems support and research and development support and charged engineering services of \$1.8 million to Point. The above financial transactions between the Company and Point are before intercompany eliminations.

As at December 31, 2005, the Company and Sokkia had collectively loaned Point U.S. \$5.3 million, the Company's share being U.S. \$2.6 million. The loans are secured by the assets of Point.

Point is dependent on the Company and Sokkia for product supply, distribution and financing. Should Sokkia and the Company discontinue their support, Point's ability to continue as a going concern would be impaired. If the existing loans to Point Inc. of U.S. \$5.3 million were ultimately not repaid by Point Inc. to the Company and Sokkia, and/or if Point, Inc. were not able to continue operations and was liquidated in an orderly wind down, the Company believes that its maximum loss exposure in the statement of operations related to Point, Inc. as of December 31, 2005, would be approximately \$600,000, comprised primarily of working capital related items and costs incurred to cease operations, after consideration of the effects of the proportionate consolidation of Point.

The consolidated financial statements of the Company included elsewhere in this Annual Report do not reflect any adjustments that would be required if Point's operations were discontinued.

## **New Canadian and U.S. GAAP Accounting Pronouncements**

### ***Canadian Pronouncements***

In January 2005, the Canadian Institute of Chartered Accountants ("CICA") issued Section 1530, "Comprehensive Income", Section 3251, "Equity", Section 3855, "Financial Instruments — Recognition and Measurement" and Section 3865, "Hedges". The new standards increase harmonization with US GAAP and will require the following:

- Financial assets will be classified as either held-to-maturity, held-for-trading or available-for-sale. Held-to-maturity classification will be restricted to fixed maturity instruments that the company intends and is able to hold to maturity and will be accounted for at amortized cost. Held-for-trading instruments will be recorded at fair value with realized and unrealized gains and losses reported in net income. The remaining financial assets will be classified as available-for-sale. These will be recorded at fair value with unrealized gains and losses reported in a new category of the consolidated balance sheet under shareholders' equity called other comprehensive income ("OCI"); and
- Derivatives will be classified as held-for-trading unless designated as hedging instruments. All derivatives, including embedded derivatives that must be separately accounted for, will be recorded at fair value on the consolidated balance sheet. For derivatives that hedge the changes in fair value of an asset or liability, changes in the derivatives' fair value will be reported in net income and be substantially offset by changes in the fair value of the hedged asset or liability attributable to the risk being hedged. For derivatives that hedge variability in cash flows, the effective portion of the changes in the derivatives' fair value will be initially recognized in OCI and the ineffective portion will be recorded in net income. The amounts temporarily recorded in OCI will subsequently be reclassified to net income in the periods when net income is affected by the variability in the cash flows of the hedged item.

The above guidance will apply for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2006. Earlier adoption will be permitted only as of the beginning of a fiscal year. The impact of implementing these new standards is not yet determinable as it is highly dependent on fair values, outstanding positions and hedging strategies at the time of adoption.

In October 2005, the Emerging Issues Committee of the CICA (the "EIC") issued Abstract No. 157, "Implicit Variable Interests Under AcG-15" (EIC-157), to address whether a company has an implicit variable interest in a VIE or potential VIE when specific conditions exist. An implicit variable interest acts the same as an explicit variable interest except it involves the absorbing and/or receiving of variability indirectly from the entity (rather than directly). The identification of an implicit variable interest is a matter of judgment that depends on the relevant facts and circumstances. EIC-157 will be effective in the first quarter of 2006. The implementation of this EIC is not expected to have a material impact on the company's consolidated financial statements.

In June 2005, the AcSB issued Handbook Section 3831, *Non-Monetary Transactions*, replacing Section 3830 of the same title. The new accounting standard requires all non-monetary transactions be measured at fair value unless certain conditions are satisfied. The new requirements are effective for non-monetary transactions initiated in periods beginning on or after January 1, 2006. The Company is in the process of evaluating the impact of the recently issued standard, but does not expect that the new standard will have a material impact on its financial position or results of operations.

### ***U.S. Pronouncements***

In December 2004, the Financial Accounting Standards Board ("FASB") issued SFAS No. 123(R), *Share-Based Payment*, which establishes accounting standards for all transactions in which an entity exchanges its equity instruments for goods and services. SFAS No. 123(R) focuses primarily on accounting for transactions with

employees. SFAS No. 123(R) eliminates the intrinsic value measurement objective in APB Opinion 25 and generally requires the Company to measure the cost of employee services received in exchange for an award of equity instruments based on the fair value of the award on the date of the grant. The standard requires grant date fair value to be estimated using either an option-pricing model which is consistent with the terms of the award or a market observed price, if such a price exists. Such cost must be recognized over the period during which an employee is required to provide service in exchange for the award in the requisite service period (which is usually the vesting period). The standard also requires the Company to estimate the number of instruments that will ultimately be issued, rather than accounting for forfeitures as they occur.

The Company is required to apply SFAS No. 123(R) beginning with its fiscal year beginning January 1, 2006. SFAS 123(R) allows for either the "modified prospective method" or the "modified retrospective method" of recognizing compensation expense. Under the modified retrospective method, the Company must restate its previously issued financial statements to recognize the amounts the Company previously calculated and reported on a pro forma basis, as if the prior standard had been adopted. Under both methods, the Company is permitted to use either a straight line or an accelerated method to amortize the costs as an expense for awards with graded vesting.

The Company currently intends to adopt SFAS No. 123(R) using the modified prospective method. The Company expects that the adoption of SFAS No. 123(R) will result in an increase to operating expenses under U.S. GAAP in 2006 of approximately \$565.

In November 2004, the FASB issued SFAS No. 151, Inventory Costs an amendment of ARB No. 43, Chapter 4, which amends Chapter 4 of ARB No. 43 that deals with inventory pricing. The Statement clarifies the accounting for abnormal amounts of idle facility expenses, freight, handling costs, and spoilage. Under previous guidance, paragraph 5 of ARB No. 43, chapter 4, items such as idle facility expense, excessive spoilage, double freight, and rehandling costs might be considered to be so abnormal, under certain circumstances, as to require treatment as current period charges. This Statement eliminates the criterion of "so abnormal" and requires that those items be recognized as current period charges. Also, this Statement requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. This Statement is effective for inventory costs incurred during fiscal years beginning after June 15, 2005, although earlier application is permitted for fiscal years beginning after the date of issuance of this Statement. Retroactive application is not permitted. Management is analyzing the requirements of this new Statement and believes that its adoption will not have any significant impact on the Company's financial position, results of operations or cash flows.

In December 2004, the FASB issued SFAS No. 153, Exchanges of Nonmonetary Assets an amendment of APB No. 29. This Statement amends Opinion 29 to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. The Statement specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. This Statement is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in fiscal periods beginning after the date this Statement is issued. Retroactive application is not permitted. The Company is analyzing the requirements of this new Statement and believes that its adoption will not have any significant impact on the Company's financial position, results of operations or cash flows.

In November 2005, the FASB issued FSP FAS 115-1 and FAS 124-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments", which nullified 2004 guidance issued by the EITF on determining whether an impairment is other-than-temporary, and effectively reverted back to previous guidance in this area. The FSP generally encompasses guidance for determining when an investment is impaired, how to measure the impairment loss, and what disclosures should be made regarding impaired securities. This FSP is effective for the first quarter of 2006 is not expected to have a material impact on the Company's consolidated financial statements.

In June 2004, the FASB issued an exposure draft of a proposed Statement, "Fair Value Measurements" to provide guidance on how to measure the fair value of financial and non-financial assets and liabilities when required

by other authoritative accounting pronouncements. The proposed statement attempts to address concerns about the ability to develop reliable estimates of fair value and inconsistencies in fair value guidance provided by current U.S. GAAP, by creating a framework that clarifies the fair value objective and its application in GAAP. In addition, the proposal expands disclosures required about the use of fair value to remeasure assets and liabilities. The standard will be effective for fiscal years beginning after December 15, 2006, and interim periods in those fiscal years, except that the disclosure requirements will be effective for fiscal years ending after December 15, 2006.

In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections", which requires that changes in accounting principle be retrospectively applied as of the beginning of the first period presented as if that principle had always been used, with the cumulative effect reflected in the carrying value of assets and liabilities as of the first period presented and the offsetting adjustments recorded to opening retained earnings. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005 with early adoption permitted. The Company is reviewing the guidance to determine the potential impact, if any, on its consolidated financial statements.

In June 2005, the FASB published an Exposure Draft containing proposals to change the accounting for business combinations. The proposed standards would replace the existing requirements of the FASB's Statement No. 141, *Business Combinations*. The proposals would result in fewer exceptions to the principle of measuring assets acquired and liabilities assumed in a business combination at fair value. Additionally, the proposals would result in payments to third parties for consulting, legal, audit, and similar services associated with an acquisition being recognized generally as expenses when incurred rather than capitalized as part of the business combination. The FASB also published an Exposure Draft that proposes, among other changes, that noncontrolling interests be classified as equity within the consolidated financial statements. The FASB's proposed standard would replace Accounting Research Bulletin No. 51, *Consolidated Financial Statements*.

On July 14, 2005, the FASB published an exposure draft entitled *Accounting for Uncertain Tax Positions* — an interpretation of FASB Statement No. 109. The proposed interpretation is intended to reduce the significant diversity in practice associated with recognition and measurement of income taxes by establishing consistent criteria for evaluating uncertain tax positions. The proposed interpretation would be effective for the first fiscal year beginning after December 15, 2006. Earlier application would be encouraged. Only tax positions meeting the probable recognition threshold at that date would be recognized. The transition adjustment resulting from application of this interpretation would be recorded as a cumulative-effect change in the income statement as of the end of the period of adoption. Restatement of prior periods or pro forma disclosures under APB Opinion No. 20, *Accounting Changes*, would not be permitted. Management is in the process of reviewing the requirements of this recent exposure draft.

On September 30, 2005, the FASB issued an Exposure Draft that would amend FASB Statement 128, *Earnings per Share*, to clarify guidance for mandatorily convertible instruments, the treasury stock method, contracts that may be settled in cash or shares and contingently issuable shares. The proposed Statement would be effective for interim and annual periods ending after June 15, 2006. Retrospective application would be required for all changes to Statement 128, except that retrospective application would be prohibited for contracts that were either settled in cash prior to adoption or modified prior to adoption to require cash settlement. Management is in the process of reviewing the requirements of this recent exposure draft.

## **Financial Instruments**

Most of the Company's revenues (over 95% in 2005) are earned in currencies other than the Canadian dollar, principally the U.S. dollar. A substantial portion of the Company's expenses, however, have been and will continue to be incurred in Canadian dollars. Accordingly, fluctuations in exchange rates between the U.S. dollar and the Canadian dollar could materially affect results of operations. In the normal course of business, the Company uses foreign currency options and forward foreign currency contracts to reduce exposure to fluctuations in the U.S. dollar to Canadian dollar exchange rates. At December 31, 2005, the Company had forward currency contracts to sell U.S. \$8.0 million between January 30, 2006 and August 31, 2006 at an average rate of \$0.8322 per Canadian dollar.

In addition, the Company had forward foreign currency contracts to sell 320,000 Euro on February 28, 2006 at a rate of 0.6677 Euro per Canadian dollar. Derivative financial instruments are not used for speculative purposes. There can be no assurance that the Company will be successful in such hedging activities.

The Company's operating budget for 2006 is based on an exchange rate of U.S. \$0.85 per Canadian dollar. The Company estimates that each \$0.01 change in the U.S. dollar to Canadian dollar exchange rate would impact the Company's 2006 budgeted net income by approximately \$500,000, prior to taking into consideration the Company's 2006 hedging program. The following table sets forth the potential impact of various hypothetical U.S. dollar to Canadian dollar exchange rates on the Company's 2006 budgeted net income, prior to taking into consideration the Company's 2006 hedging program.

<u>U.S. \$ per Canadian \$</u>	<u>Impact on 2006 Budgeted Net Income</u>
	<u>Favourable/(Unfavourable)</u> <u>(CDN\$)</u>
\$0.81 .....	\$2.2 million
\$0.82 .....	\$1.6 million
\$0.83 .....	\$1.1 million
\$0.84 .....	\$0.5 million
\$0.85 .....	—
\$0.86 .....	\$(0.5) million
\$0.87 .....	\$(1.0) million
\$0.88 .....	\$(1.5) million
\$0.89 .....	\$(2.0) million
\$0.90 .....	\$(2.5) million
\$0.91 .....	\$(2.9) million
\$0.92 .....	\$(3.4) million
\$0.93 .....	\$(3.8) million

The Company is not subject to significant interest rate risk due to the short-term maturities of the Company's outstanding loans and short term investments.

#### **A. Inflation**

While the Company believes that inflation has not had a material effect on its results of operations, there can be no assurance that inflation will not have such an effect in the future.

#### **B. Liquidity and Capital Resources**

See "Item 5 — Operating and Financial Review and Prospects, Liquidity and Capital Resources."

#### **C. Research and Development, Patents and Licences, etc.**

See "Item 4 — Information on the Company, Business Overview — Research and Development" and "— Patents, Trademarks and Licenses."

#### **D. Trend Information**

See "Item 5 — Operating and Financial Review and Prospects, Operating Results."

#### **E. Off Balance Sheet Arrangements**

See "Item 5 — Operating and Financial Review and Prospects, Operating Results — Off Balance Sheet Arrangements."

## F. Tabular Disclosure of Contractual Obligations

See “Item 5 — Operating and Financial Review and Prospects, Operating Results — Contractual Obligations.”

## Item 6. Directors, Senior Management and Employees

### A. Directors and Senior Management

The following table sets forth certain information, as of March 15, 2006, regarding the executive officers, directors and certain key employees of the Company:

Name	Age	Position	Director Since	Executive Officer Since
<b>Directors, Executive Officers and Key Employees</b>				
Jonathan W. Ladd .....	50	President and Chief Executive Officer	2002	2002
Werner Gartner .....	49	Executive Vice President and Chief Financial Officer	2001	1995
Patrick C. Fenton .....	48	Vice President and Chief Technology Officer	2005	2003
Farlin A. Halsey, Jr. ....	40	Vice President, Marketing	—	2003
Anthony J. Murfin .....	58	Vice President, Business Development	—	—
Graham C. Purves .....	43	Vice President, Sales	—	2003
Michael McAloney .....	48	Vice President, Operations and Quality	—	—
Curtis Anderson .....	45	Vice President, OEM Product Development	—	—
Robert J. Iverach .....	58	Director	2005	—
Richard D. Orman .....	57	Vice Chairman of the Board	1994	—
Joel A. Schleicher .....	54	Director	1997	—
Charles R. Trimble .....	64	Director	2002	—
David E. Vaughn .....	60	Chairman of the Board	2001	—

The following is a brief biography of each of the directors and officers of the Company, which includes a description of their present occupation and their principal occupations during at least the past five years.

*Jonathan W. Ladd.* Mr. Ladd was appointed President and Chief Executive Officer of the Company in February 2002 and has served as a director of the Company from July 2002. From July 2001 to November 2001, Mr. Ladd served as Senior Vice President, Engineering at Thales Navigation Inc., a satellite positioning product company, and President of Thales’ Russian subsidiary, Ashtech A/O. From January 1998 to July 2001, Mr. Ladd served in several other management positions at Magellan Corporation, a satellite positioning product company, including Senior Vice President, Advanced Technology Group and Vice President and General Manager of Ashtech Precision Products Business Unit.

*Werner Gartner.* Mr. Gartner was appointed Executive Vice President and Chief Financial Officer of the Company in October 1996 and has served as a director of the Company from July 2001. Mr. Gartner also served as a director of the Company from November 1995 until May 1998. From November 2000 to February 2001, Mr. Gartner, in addition to his regular duties, served as Acting Interim President and Chief Executive Officer of the Company. From August 1990 to October 1996, Mr. Gartner served in a variety of financial positions at the Company including Vice President, Finance and Corporate Controller.

*Patrick C. Fenton.* Mr. Fenton was appointed Chief Technology Officer in January 2002 and became an executive officer of the Company in April 2003. Mr. Fenton previously served as Vice President, Technology of the Company from October 1998 and as Vice President, Research and Development of the Company from March 1997 until October 1998. Mr. Fenton previously served as Director, Research and Development for NovAtel’s GPS business unit from February 1995 until March 1997 and was Chief Engineer for the GPS business unit from November 1993 to February 1995. Mr. Fenton was appointed to the board of directors in March 2005.

*Farlin A. Halsey, Jr.* Mr. Halsey was appointed Vice President, Marketing of the Company in July 2002. From August 2000 to January 2002, Mr. Halsey served as Vice President of Marketing for JP Mobile, a mobile server company. From August 1999 to August 2000, Mr. Halsey served as Director of Marketing-Personal Navigation with Navigation Technologies Company, a provider of digital mapping databases. From March 1993 to August 1999, Mr. Halsey served in various sales and marketing positions for Topcon America Company.

*Anthony J. Murfin.* Mr. Murfin was appointed Vice President, Business Development of the Company in April 2002. Mr. Murfin has also served as Director, Aviation Group of the Company from April 1998 until April 2002. Mr. Murfin previously served as Director, Corporate Accounts of the Company from April 1995 to April 1998 and as Director of Product and Marketing of the Company from April 1994 to April 1995. From January 1980 to April 1994, Mr. Murfin served in various capacities including Business Development Manager and Product Manager (Flight Systems) in the Avionics Division of CMC Electronics. From September 1977 until January 1980, Mr. Murfin was employed by CAE Electronics, a provider of advanced simulation technologies.

*Graham C. Purves.* Mr. Purves was appointed Vice President, Sales of the Company in January 2002. Mr. Purves previously served as Vice President, Sales and Marketing of the Company from October 1998 to January 2002. Mr. Purves assumed additional responsibility for product development in July 1999. Mr. Purves previously served as Director, Custom Products Group for the Company from January 1998 until October 1998, and as Director, Business Operations for the Company's GPS business unit from September 1994 until October 1998. From August 1988 to September 1990, Mr. Purves served in various capacities at the Company including Manager, VLSI Design Group.

*Curtis Anderson.* Mr. Anderson was appointed Vice President, OEM Product Development in January 2005. Mr. Anderson previously served as Director, OEM Engineering from February 2000 until January 2005. Since joining NovAtel in 1994, Mr. Anderson served in a variety of product development roles, including Firmware Engineer and Project Manager.

*Michael McAloney.* Mr. McAloney was appointed Vice President, Business Operations and Corporate Quality in March, 2005. Mr. McAloney previously served as Director, Technical Services and Business Operations from 2002 to 2005 and Director Technical Services from 1998 to 2002. From 1995 to 1998, Mr. McAloney was Programs Manager for NovAtel's GPS business unit. Mr. McAloney is currently a Director of Canadian Manufacturers and Exporters Alberta. Prior to joining NovAtel, Mr. McAloney was employed as Systems Engineer Manager at Micronav Ltd., a provider of Microwave Landing Systems.

*Robert J. Iverach.* Mr. Iverach was appointed as a director of the Company in March 2005. From January 1994 to December 2004, Mr. Iverach was a Partner with Felesky Flynn LLP, a tax law firm in Calgary, Alberta. From January 2005 to December 2005, Mr. Iverach was Counsel with that firm. He retired completely from Felesky Flynn LLP on December 31, 2005. Mr. Iverach is presently the Chairman of Win Energy Corporation, Chairman of RAMTelecom Inc, a director of Vacchi-Test Corporation, and a Trustee of Big Eagle Services Trust.

*Richard D. Orman.* Mr. Orman has served as Vice Chairman of the board of directors of the Company since March 1997 and as a director of the Company since January 1994. Mr. Orman currently serves as Chief Executive of Nor Energy AS. From March 2003 to September 2005, he served as Executive Vice-Chairman of Exceed Energy Inc. From June 1999 to April 2003, Mr. Orman served as Chairman and Chief Executive Officer of Hemisphere International Inc. From March 1996 to October 1998, Mr. Orman was Chairman and Chief Executive Officer of Kappa Energy Company Inc. and served as a director until January 2000. From May 1986 to December 1992, Mr. Orman served as a member of the Alberta legislature and as Minister of Employment from May 1986 to September 1988, Minister of Labour from September 1988 to April 1989 and Minister of Energy from April 1989 to December 1992. Mr. Orman is lead director for Daylight Energy, a company listed on the Toronto Stock Exchange. Mr. Orman has also served as a director of a number of other public companies.

*Joel A. Schleicher.* Mr. Schleicher has served as a director of the Company since March 1997. Mr. Schleicher currently serves as Chairman and Chief Executive Officer for Integrated Solutions, Inc. From June 2000 to July 2002, Mr. Schleicher served as Chairman and Chief Executive Officer of Interpath Communications Inc. (prior to

their acquisition of USinternetworking, Inc.) and continues to serve on its board. Mr. Schleicher served as Chairman and Chief Executive Officer of Expanets, Inc. from June 1998 to January 2000. Mr. Schleicher served as a business consultant, advisor and investor with and to private equity firms from July 1997 to June 1998. From June 1996 to June 1997, Mr. Schleicher served as President and Chief Executive Officer of ProCommunications, Inc. From July 1995 to June 1996, Mr. Schleicher was a private investor. From 1989 to July 1995, Mr. Schleicher served as Chief Operating Officer of and a board member for Nextel Communications, Inc. Mr. Schleicher also serves as a Director of TechTronic Industries Co. Ltd.

*Charles R. Trimble.* Mr. Trimble has served as a director of the Company since January 2002. Mr. Trimble currently serves as Chairman of the United States GPS Industry Council. Mr. Trimble also serves as a Director of KVH Industries, Inc. Mr. Trimble was one of the founders of Trimble Navigation Limited, a provider of GPS and other positioning technologies and products, in 1978 and served as President, Chief Executive Officer and a director of such company from 1981 to 1998.

*David E. Vaughn.* Mr. Vaughn has served as a director of the Company since July 2001 and was elected Chairman of the board of directors in March 2004. Mr. Vaughn also served as President and Chief Executive Officer of the Company from February 2001 to February 2002. Mr. Vaughn currently serves as President of Foursome Technologies, a consulting firm. From January 1999 to December 2000, Mr. Vaughn served as Senior Vice President and Chief Operations Officer with Magellan Corporation. Also with Magellan Corporation, Mr. Vaughn served as Senior Vice President, Strategic Business Alliances from August 1998 to January 1999. From June 1991 to July 1998, Mr. Vaughn served with Trimble Navigation Limited, a provider of GPS and other positioning technologies and products, in a variety of positions including Executive Vice President, Tracking and Communications Products Division and, most recently, as Executive Vice President, Corporate Business Development.

There is no family relationship between any of the directors and the executive officers. There are no arrangements or understandings between any director or executive officer and any other person pursuant to which any director and executive officer was selected.



## B. Compensation

### Summary of Executive Compensation

The following table provides a summary of the compensation paid during each of the three most recently completed fiscal years to each of the Chief Executive Officer and the four next most highly compensated executive officers of the Company who are currently serving as executive officers of NovAtel and whose total salary and other compensation during the fiscal year ended December 31, 2005 exceeded U.S. \$100,000 (the "Named Executive Officers").

Name and Principal Position	Year	Annual Compensation			Long Term Compensation			
		Salary (\$)	Bonus (\$)	Other Annual Compensation (\$)	Awards		Payouts	
					Restricted Stock Awards (\$)	Securities Under Options/ SARs Granted (#)	LTIP Payouts (\$)	All Other Compensation (\$)
Jonathan W. Ladd ..... CEO and President	2005	\$ 299,369	\$ 242,500	\$14,917(2)	—	14,500	—	—
	2004	\$ 294,595	\$ 329,754	\$14,198(2)	\$ 71,500(3)	—	—	—
	2003	\$ 282,383	\$ 176,148	\$14,674(2)	—	50,000	—	\$6,079(1)
Werner Gartner ..... Executive Vice President and CFO	2005	\$ 193,114	\$ 132,015	\$ 9,656(2)	—	7,000	—	—
	2004	\$ 185,567	\$ 161,992	\$ 9,266(2)	\$ 36,036(3)	—	—	—
	2003	\$ 177,902	\$ 79,176	\$ 9,129(2)	—	15,000	—	—
Patrick C. Fenton ..... Chief Technology Officer	2005	\$ 168,089	\$ 110,090	\$ 8,405(2)	—	6,200	—	—
	2004	\$ 160,696	\$ 140,290	\$ 8,025(2)	\$ 31,200(3)	—	—	—
	2003	\$ 154,027	\$ 68,551	\$ 8,004(2)	—	12,500	—	—
Farlin A. Halsey ..... Vice President, Marketing	2005	\$ 162,989	\$ 101,024	\$ 8,149(2)	—	5,000	—	—
	2004	\$ 158,744	\$ 134,068	\$ 7,930(2)	\$ 23,288(3)	—	—	—
	2003	\$ 153,524	\$ 62,100	\$ 7,967(2)	—	9,000	—	—
Graham C. Purves ..... Vice President, Sales	2005	\$ 160,721	\$ 101,024	\$ 7,911(2)	—	5,000	—	—
	2004	\$ 149,432	\$ 134,068	\$ 7,371(2)	\$ 21,840(3)	—	—	—
	2003	\$ 143,759	\$ 72,800	\$ 7,344(2)	—	10,500	—	—
All directors and executive officers as a group (ten in 2005, twelve persons in 2004, and twelve persons in 2003)	2005	\$1,265,600	\$ 686,653	\$49,038	—	43,855	—	—
	2004	\$1,283,333	\$1,034,240	\$53,821	\$205,219	—	—	—
	2003	\$1,172,999	\$ 517,900	\$54,022	—	107,500	—	\$6,079

- (1) Represents total relocation costs paid by the Company.
- (2) Represents matching contributions made by the Company on behalf of each Named Executive Officer into their respective Registered Retirement Savings Plans.
- (3) Represents values for awards of phantom share units issued pursuant to the 2004 Employee Long-term Incentive Plan. The value of the units are payable in cash subject to performance vesting conditions. Vesting will occur on December 31, 2006 if the cumulative revenue and operating income for the three years ending December 31, 2006 exceeds certain pre-determined performance objectives. As of December 31, 2005, the following number and value of the phantom stock units were held by each executive officer listed in the table: Ladd (5,730 units, U.S.\$166,686); Gartner (2,888 units, U.S. \$84,012); Fenton (2,500 units, U.S. \$72,725); Halsey (1,866 units, U.S. \$54,282); and Purves (1,750 units, U.S. \$50,908). No dividends are paid on phantom share units. The plan will be liquidated and amounts payable to the participants will be paid out in the event of a change of control of NovAtel based on the months of completed service and the relative success in achieving the performance targets.

### Options Granted During the Year Ended December 31, 2005

The following table sets forth the details of all options to purchase Common Shares that were granted to the named Executive Officers during the fiscal year ended December 31, 2005.

<u>Name</u>	<u>Securities Under Options/SARs Granted (#)</u>	<u>% of Total Options/ SARs Granted to Employees in Financial Year (%)</u>	<u>Exercise or Base Price (U.S.\$/Security)</u>	<u>Grant Date Present Value (U.S.\$) <sup>(1)</sup></u>	<u>Expiration Date</u>
Jon Ladd, ..... President and CEO	14,500	13.0%	\$19.61	\$132,675	May 12, 2010
Werner Gartner, ..... Executive VP and CFO	7,000	6.3%	\$19.61	\$ 64,050	May 12, 2010
Pat Fenton, ..... Chief Technology Officer	6,200	5.5%	\$19.61	\$ 56,730	May 12, 2010
Farlin Halsey ..... VP, Marketing	5,000	4.5%	\$19.61	\$ 45,750	May 12, 2010
Graham Purves, ..... VP, Sales	5,000	4.5%	\$19.61	\$ 45,750	May 12, 2010

(1) Based on a Black- Scholes option pricing model. The same model is used to compute the compensation expense related to stock options reported in the Company's financial statements.

### Options Exercised During the Year Ended December 31, 2005

The following table sets forth details of: (i) options exercised, and the value thereof, by the Named Executive Officers during the fiscal year end December 31, 2005, (ii) the number of unexercised options as at December 31, 2005 (exercisable and unexercisable) held by the Named Executive Officers and (iii) the value of unexercised "in-the-money" options as at the fiscal year ended December 31, 2005, (exercisable and unexercisable) held by the Named Executive Officers. The closing price of the Company's common shares on the last trading day of the fiscal year was U.S. \$27.54 per share.

<u>Name</u>	<u>Securities Acquired on Exercise</u>	<u>Aggregate Value Realized (U.S. \$)</u>	<u>Unexercised Options December 31, 2005 (Exercisable/Unexercisable)</u>	<u>Value of Unexercised In-the-Money Options at December 31, 2005 (Exercisable/Unexercisable) (U.S. \$)</u>
Jonathan W. Ladd ..... CEO and President	—	—	20,000/47,000	\$503,925/\$935,035
Werner Gartner ..... Executive Vice President & CFO	40,000	\$660,414	61,250/18,250	\$1,335,023/\$340,023
Patrick C. Fenton ..... Chief Technology Officer	5,100	\$134,929	70,025/14,950	\$1,176,817/\$270,453
Farlin A. Halsey ..... Vice President, Marketing	—	—	11,000/14,500	\$270,965/\$275,655
Graham C. Purves ..... Vice President, Sales	10,000	\$226,918	21,923/12,125	\$456,025/\$172,423

NovAtel's Employee Stock Option Plan and Directors Stock Option Plan (collectively, the "Plans") authorize the grant of options to purchase Common Shares to employees or directors of NovAtel or employees of a related company and non-employee directors of NovAtel, respectively.

Each of the Plans may be administered by either NovAtel's board of directors or by a committee established by the board of directors. A committee established by the board of directors to administer the Employee Stock Option Plan must include at least one director of the Company.

The Employee Stock Option Plan provides for the granting of stock options ("Options") to employees and to such other persons that have or will provide some service to the Company or a related company. The purpose of the Employee Stock Option Plan is to attract and retain the best available personnel for positions of substantial responsibility. The Employee Stock Option Plan is administered by the Compensation Committee of the Board of Directors.

The price of the Company's Common Shares subject to each Option (the "Option Price") is set by the Compensation Committee and shall not be less than 100% of the fair market value per Common Share. The Compensation Committee set an Option Price of 115% of fair market for option grants made in May 2005. Options granted under the Employee Stock Option Plan are exercisable at the times and on the terms established by the Compensation Committee. The Compensation Committee may accelerate the exercisability of any Option. Options may also be accelerated in the event the Company is liquidated or dissolved or if certain conditions are met with respect to a change of control.

Vested Options terminate 90 days after an optionee's termination for any reason other than death or disability. Unvested Options terminate immediately upon the termination of an optionee's employment or service to the Company. Unless provided otherwise by the Compensation Committee, all Options granted, except incentive stock options, shall expire ten years from the date of grant. The expiration date shall not be later than ten years from the date of grant for incentive stock options. However, any Option granted to a greater than ten percent shareholder of the Company shall not be exercised later than five years from the date of grant. The Compensation Committee set an Option expiration date of five years from the date of grant for Options granted in May 2005. No incentive stock options have been granted. The Option Price must be paid in full in cash or its equivalent at the time of exercise. The Compensation Committee may also permit payment of the Option Price by the tender of previously acquired Common Shares of the Company or such other mechanism approved by the Compensation Committee from time to time.

The June 2005 amendments to the Employee Stock Option Plan also provide that the minimum exercise price of stock options be no less than 100% of the fair market value on the date of grant, that neither the Board of Directors nor the Compensation Committee be authorized to materially amend the Employee Stock Option Plan without shareholder approval; and re-pricing of stock options (including the cancellation and exchange of options) not be permitted without shareholder approval. In addition, the number of Common Shares available for future grant, together with the number of Common Shares issuable upon exercise of outstanding options under the Employee Stock Option Plan and the Directors Stock Option Plan, collectively, may not exceed 13% of the Common Shares outstanding at any time.

The Directors Option Plan provides for the granting of stock options ("Directors Options") to eligible non-employee directors of the Company. The purpose of the Directors Option Plan is to attract and retain the best available persons for positions on the Company's Board of Directors. The Directors Option Plan is administered by the Compensation Committee of the Board of Directors.

Under the amended Directors Option Plan, each non-employee director automatically will receive upon joining the Board of Directors and on the date of each subsequent annual meeting at which he or she is a non-employee director, a Directors Option to purchase such number of Common Shares as determined by dividing U.S. \$40,000 by the fair market value of a Common Share on the date of the annual meeting in question. Any fractional share will be rounded up to the next full share. For purposes of the Directors Option Plan, fair market value on any date means the closing selling price for a Common Share on The NASDAQ Stock Market on that date.

For example, if the fair market value of a Common Share on the date of the annual meeting in question was U.S. \$25.00, then the non-employee director would receive a Directors Option to purchase 1,600 shares (i.e. U.S. \$40,000 divided by U.S. \$25.000).

The exercise price of the shares subject to each Directors Option will be 100% of the fair market value of the shares on the date of grant. Each Directors Option will become exercisable one year from the date of grant of the Directors Option; provided however that if prior to such date the participant terminates his or her service

on the Board of Directors on account of death or disability, then the Directors Option will become exercisable in full on the date of such termination of service. Each Directors Option will terminate five years from the date of grant of the Directors Option. In addition, each Directors Option provides that, until the non-employee director resigns or does not stand for re-election, a non-employee director may only sell up to 50% of the shares received upon exercise of a Directors Option.

The June 2005 amendments to the Directors Option Plan also provide that discretionary grants to non-employee directors be replaced with annual non-discretionary grants pursuant to the terms of the plan; that neither the Board of Directors nor the Compensation Committee be authorized to materially amend the Directors Option Plan without shareholder approval; and that re-pricing of stock options (including the cancellation and exchange of options) not be permitted without shareholder approval. In addition, the number of Common Shares available for future grant, together with the number of Common Shares issuable upon exercise of outstanding options under the Employee Stock Option Plan and the Directors Stock Option Plan, collectively, may not exceed 13% of the Common Shares outstanding at any time.

The vesting schedule for each option granted pursuant to the Plans is specified by the board of directors or the committee, as the case may be, at the time of the grant. The vesting of outstanding options may be accelerated by the board of directors or the committee, as the case may be, at such times and in such amounts as the board of directors or the committee, as the case may be, determines in its sole discretion. Options that have been outstanding for at least six months immediately vest upon a change of control and are fully exercisable for a specified number of days depending on the nature of the event resulting in a change of control.

Options granted under the Plans are non-transferable. Vested options granted under each of the Plans terminate on the earlier of: (i) the expiry of the option (as discussed above); (ii) the expiry of 90 days from the date that an optionee ceases to be employed by or a member of the board of directors of the Company, as the case may be, for reasons other than death or disability; and (iii) the expiry of one year from the date of death of an optionee or the date that an optionee ceases to be employed by or a member of the board of directors of the Company, as the case may be, by reason of disability.

#### **2004 Employee Long-term Incentive Plan**

In February 2005, the board of directors approved the 2004 Employee Long-term Incentive Plan ("LTI Plan") which authorizes the grant of phantom shares to management and employees of the Company. The board of directors is ultimately responsible for the LTI Plan and has designated overall responsibility for the LTI Plan to the Compensation Committee. The number of phantom shares issued and outstanding as of December 31, 2005, was approximately 43,000, which if paid out on December 31, 2005, would have had a value of \$1.4 million.

All grants made under the LTI Plan will have a three-year term ending on December 31, 2006. Grants are subject to performance vesting conditions. Vesting will occur on December 31, 2006, if pre-set performance objectives for revenue and operating income are satisfied. Payments with respect to each grant under the LTI Plan will be made in cash, on or about March 31, 2007, subject to approval of the December 31, 2006 year end audited financial results. The value of a phantom share at the time of payment will be based on a 20-day average of the closing price of NovAtel common shares.

The LTI Plan will be liquidated and amounts payable to participants will be paid out in the event of a change of control of NovAtel. The amount payable will be pro rated based on months of completed service within the LTI Plan term and relative success in achieving the performance targets to the most recently completed quarter.

#### **Management Employment Contracts**

Jonathan W. Ladd, Werner Gartner and Patrick C. Fenton have employment-related contracts which provide for, among other things, industry standard covenants in the Company's favour, including non-competition covenants for one year following termination. The contracts also provide that the Company can terminate an officer without

cause upon which event the officer is entitled to one times his annual salary plus accelerated vesting of certain options, depending on the agreement. In addition, the contracts contain provisions relating to payments and accelerated vesting of stock options upon a termination within a certain amount of time of a change of control of the Company, with payments ranging from one and one-half to two times salary, depending on the contract.

### **Summary of Directors' Compensation**

Directors do not have service contracts with the Company. NovAtel compensates its directors who are not employees of the Company a base amount of \$20,000 per year. The Chairman of the Board receives an additional \$20,000 per year. Additional payments of \$10,000 annually are paid to both the chairman and all members of the Audit Committee. The chairman of the Audit Committee receives an additional \$10,000. In addition, directors are paid \$1,000 for attendance at meetings of the board of directors, the Compensation Committee and the Audit Committee, with an additional \$200 per hour payable for attendance at all supplemental meetings.

The directors of the Company received an aggregate of 6,155 stock options of NovAtel as compensation for their services in 2005 (nil in 2004 and 2003).

### **Directors' and Officers' Liability Insurance**

The Company maintains a comprehensive directors' and officers' liability policy for events arising prior to CMC Electronics acquiring majority control of the Company on April 17, 1998. This policy was originally purchased for \$42,000 for the policy period from December 1, 2000 to December 1, 2005 and extended to March 31, 2007. The policy covers limits of liability for each loss and for each policy period of \$10 million with a \$250,000 deductible for any claims.

CMC Electronics, our former majority shareholder, maintains a comprehensive directors' and officers' liability policy for events arising subsequent to April 17, 1998 and prior to April 12, 2001. This policy was purchased for the period April 1, 2001 to April 1, 2007. Directors and officers of the Company are covered by this policy which covers limits of liability for each loss and for the policy period of \$35 million with a \$250,000 deductible for U.S. securities related claims and \$100,000 deductible for other claims.

Onex Corporation, which controls directly or indirectly, a majority of the common shares of CMC Electronics, maintains a comprehensive directors' and officers' liability policy which applies to the Company's directors and officers for events arising subsequent to April 12, 2001 and prior to February 3, 2005. The Onex Corporation policy is in place until November 29, 2006.

The Company maintains comprehensive directors' and officers' liability policies for events arising subsequent to January 27, 2005. These policies, in place until April 30, 2007, cover limits of liability for each loss and for each policy period of U.S. \$10 million primary coverage with a U.S. \$250,000 deductible for any claims and U.S. \$10 million excess coverage. The annual premium for these policies is U.S. \$217,850.

### **Indebtedness of Directors and Executive Officers**

No executive officers or directors of NovAtel, or any of their associates or affiliates, are or have been indebted to NovAtel since the commencement of the last completed financial year of the Company, nor have any of the foregoing been the subject of a guarantee, support agreement, letter of credit or other similar arrangement or understanding provided by NovAtel or any of its subsidiaries since the commencement of the last completed financial year.

### **C. Board Practices**

All directors hold office until the next annual meeting of the Company's shareholders, which has been in July for the past several years, or until their respective successors are duly appointed by the Board of Directors or their positions are earlier vacated by resignation or otherwise.

Executive officers are appointed by the board of directors on an annual basis and serve until the next annual meeting of the board of directors or until their respective successors are duly appointed or their positions are earlier vacated by resignation or otherwise.

### **Committees of the Board of Directors**

The Company has an Audit Committee and a Compensation Committee.

#### ***Audit Committee***

The Audit Committee assists the board of directors of the Company in fulfilling its responsibilities for oversight and supervision of financial and accounting matters. The Audit Committee responsibilities include the engagement or discharge of independent auditors, review with the independent auditors the plan and results of the auditing engagement, review NovAtel's internal auditing procedures, system of internal accounting controls and financial management and to make inquiries into matters within the scope of this Committee's functions. The members of the Audit Committee are Richard D. Orman, Joel A. Schleicher and Charles R. Trimble. The Board of Directors has determined that all members of the Audit Committee are "independent directors" as determined in accordance with applicable securities laws and rules of the National Association of Securities Dealers (NASD). The board of directors and the Audit Committee have adopted a written charter of the Audit Committee. The Audit Committee reviews and assesses the adequacy of the charter on an annual basis.

#### ***Compensation Committee***

The function of the Compensation Committee is to ensure that the Company has a high caliber executive management in place and a total compensation plan that is competitive, motivating and rewarding for participants. The Compensation Committee reviews and makes recommendations to the board of directors of the Company concerning the compensation of the key management employees of the Company and the administration of the Plans. The members of the Compensation Committee are Richard D. Orman, Robert Iverach and David E. Vaughn. The Board of Directors has determined that each member of the Compensation Committee is an "independent director" as determined in accordance with applicable securities laws and NASD rules.

### **D. Employees**

See "Item 4 — Information on the Company, Business Overview — Employees."

## E. Share Ownership

The following table sets forth as of March 21, 2006, the ownership of the Company's Common Shares by each director and Named Executive Officer, listed in the compensation table above, and all directors and executive officers as a group:

<u>Name</u>	<u>Shares Beneficially Owned</u>	
	<u>Shares</u>	<u>Percent</u>
Patrick C. Fenton (1) .....	75,650	*
Werner Gartner (2) .....	66,750	*
Farlin A. Halsey (3) .....	10,000	*
Robert J. Iverach .....	5,000	*
Jonathan W. Ladd (4) .....	60,000	*
Richard D. Orman .....	—	—
Graham C. Purves (5) .....	26,423	*
Joel A. Schleicher (6) .....	5,250	*
Charles R. Trimble (7) .....	7,000	*
David E. Vaughn .....	—	—
All directors and executive officers as a group (ten persons) (8) .....	<u>256,073</u>	<u>3.0</u>

\* Less than 1%.

(1) Represents vested stock options to purchase 75,650 Common Shares of the Company as of March 21, 2006.

(2) Includes vested stock options to purchase 48,750 Common Shares of the Company as of March 21, 2006.

(3) Represents vested stock options to purchase 10,000 Common Shares of the Company as of March 21, 2006.

(4) Includes vested stock options to purchase 40,000 Common Shares of the Company as of March 21, 2006.

(5) Represents vested stock options to purchase 26,423 Common Shares of the Company as of March 21, 2006.

(6) Represents vested stock options to purchase 5,250 Common Shares of the Company as of March 21, 2006.

(7) Represents vested stock options to purchase 7,000 Common Shares of the Company as of March 21, 2006.

(8) Includes vested stock options to purchase 213,073 Common Shares of the Company as of March 21, 2006.

## Item 7. Major Shareholders and Related Party Transactions

### A. Major Shareholders

The following table sets forth as of March 20, 2006 those persons known to the Company to be owners of more than 5% of the Common Shares:

	Shares Beneficially Owned	
	Shares	Percent
FMR Corp. (1) .....	600,000	7.3%
Provident Investment Counsel (2) .....	569,859	6.8%
Essex Investment Management Co., LLC (3) .....	424,699	5.1%

(1) The address of FMR Corp. is 82 Devonshire Street, Boston, Massachusetts, USA, 02109.  
Based on a Schedule 13 G/A filed on February 14, 2006.

(2) The address of Provident Investment Counsel is 300 North Lake Avenue, Suite 1001, Pasadena, California, USA, 91101-4106.  
Based on a Schedule 13 G filed on January 10, 2006.

(3) The address of Essex Investment Management Co., LLC is 125 High St., 29<sup>th</sup> Floor, Boston, Massachusetts, USA, 02110.  
Based on a Schedule 13G filed on February 9, 2006.

To the best of the Company's knowledge, as of April 3, 2006, U.S shareholders held approximately 5,586,000 of the Company's outstanding common shares, or 66.3% of total common shares outstanding. This figure may not be entirely accurate because the Company can obtain only limited information regarding the current holding of the Company's shares in the United States. As of April 3, 2006, there were 21 registered shareholders of NovAtel, of which 19 have addresses within the United States.

### B. Related Party Transactions

See "Item 5 — Operating and Financial Review and Prospects, Operating Results — Related Party Transactions" and "Item 4 — Information on the Company, Business Overview — Strategic Partnerships — CMC Electronics" and "— Certain Contractual Rights."

### C. Interests of Experts and Counsel

Not applicable.

## Item 8. Financial Information

### A. Consolidated Statements and Other Financial Information

#### Consolidated Financial Statements

See Item 18 "Financial Statements" for a full list of financial statements included as part of this Annual Report.

#### Legal Proceedings

See "Item 4 — Information on the Company, Business Overview — Legal Proceedings."



## Dividend Policy

The Company has not declared or paid any dividends on the Common Shares to date. The payment of dividends in the future will be dependent on the earnings and financial condition of the Company and on such other factors as the board of directors of NovAtel considers appropriate.

### B. Significant Changes

Not applicable.

## Item 9. The Offer and Listing

### A. Offer and Listing Details

The Company's Common Shares have been listed on The Nasdaq Stock Market since February 7, 1997. The following are the price ranges as reported by The Nasdaq Stock Market for the periods indicated.

	U.S. \$	
	High	Low
<b>Annual</b>		
2005 .....	\$48.450	\$14.318
2004 .....	\$50.350	\$ 8.070
2003 .....	\$11.080	\$ 1.900
2002 .....	\$ 5.200	\$ 1.760
2001 .....	\$ 3.050	\$ 1.250
<b>Quarterly</b>		
Q4 - 2005 .....	\$31.760	\$21.690
Q3 - 2005 .....	\$37.150	\$22.910
Q2 - 2005 .....	\$29.190	\$14.318
Q1 - 2005 .....	\$48.450	\$16.260
Q4 - 2004 .....	\$50.350	\$11.390
Q3 - 2004 .....	\$14.990	\$ 8.540
Q2 - 2004 .....	\$15.470	\$ 9.500
Q1 - 2004 .....	\$18.900	\$ 8.070
<b>Monthly</b>		
April 2006 .....	\$37.290	\$34.250
March 2006 .....	\$37.610	\$31.810
February 2006 .....	\$35.450	\$30.510
January 2006 .....	\$35.140	\$26.910
December 2005 .....	\$30.870	\$26.660
November 2005 .....	\$31.760	\$27.560
October 2005 .....	\$29.400	\$21.690

### B. Plan of Distribution

Not applicable.

### C. Markets

In February 1997, the Company's Common Shares commenced trading in the United States on the Nasdaq National Market tier of The Nasdaq Stock Market under the symbol "NGPSF." The Common Shares are not listed on any other non-United States trading market. On March 15, 1999, the Company's symbol was changed to "NGPS."

Prior to February 4, 1997, the Company's Common Shares were not listed on any trading market.

#### **D. Selling Shareholders**

Not applicable.

#### **E. Dilution**

Not applicable.

#### **F. Expenses of the Issue**

Not applicable.

### **Item 10. Additional Information**

#### **A. Share Capital**

Not applicable.

#### **B. Articles of Incorporation**

The Company is registered under the *Canada Business Corporations Act* ("CBCA" or the "Act") as corporation number 076226-1 and has the capacity and, subject to the provisions of the Act, the rights, powers and privileges of a natural person.

#### **Powers of Directors**

Subject to any unanimous shareholder agreement, the directors shall manage or supervise the management of the business and affairs of the Company and may exercise all such powers and do all such acts and things as may be exercised or done by the Company and are not by the Act, the articles, the by-laws, any special resolution of the Company, a unanimous shareholder agreement or by statute expressly directed or required to be done in some other manner. Notwithstanding any vacancy among the directors, the remaining directors may exercise all the powers of the board so long as a quorum of the board remains in office.

The Act requires every director or officer who is a party to a material contract or a material transaction, whether made or proposed with the Company, or who is a director or officer of or has a material interest in any person who is a party to a material contract or a material transaction, whether made or proposed contract with the Company to disclose in writing to the Company or request to have entered in the minutes of meetings of directors or meetings of committees of directors the nature and extent of his or her interest, and shall, except in certain limited circumstances, refrain from voting in respect of the material contract or material transaction. The articles and by-laws do not require an independent quorum to enable the directors to vote compensation to themselves or any member of their body. The Act also provides that the shareholders of the Company may examine the portion of any minutes of meetings of directors or such other documents that contain such disclosures of interest.

Unless the articles or by-laws of or a unanimous shareholder agreement relating to the Company otherwise provide, the directors of the Company may, without authorization of the shareholders, (a) borrow money on the credit of the Company, (b) issue, reissue, sell, pledge or hypothecate debt obligations of the Company, (c) to the extent permitted by the CBCA, give a guarantee on behalf of the Company to secure performance of an obligation by any person, and (d) mortgage, hypothecate, pledge or otherwise create a security interest in all or any property of the Company, owned or subsequently acquired, to secure any obligation of the Company. The Company does not have a unanimous shareholder agreement and the Company's articles and by-laws do not limit the above powers.

Directors of the Company are not required to own shares of the Company in order to qualify as a director and the directors are not required to retire upon reaching a specified age.

## **Description of Securities**

The Company is authorized to issue an unlimited number of Common Shares and an unlimited number of First Preference Shares.

Holders of Common Shares are entitled to receive notice of and to attend all meetings of the shareholders of the Company, except meetings at which holders of another specified class of shares are exclusively entitled to vote, and are entitled to one vote for each Common Share held on all votes taken at such meetings. The holders of Common Shares are entitled to receive such dividends as the directors may in their discretion declare, regardless of whether dividends are declared on any other class of shares. Upon liquidation, dissolution or wind-up of the Company, the holders of Common Shares are entitled to receive any remaining property after payment of any amount required to redeem or retract the issued and outstanding First Preference Shares.

The First Preference Shares may be issued in one or more series with each series to consist of such number of shares as may, before the issue of the series, be fixed by the directors of the Company. The directors are authorized, before the issue of the series, to determine the designation, rights, privileges, restrictions and conditions attaching to the First Preference Shares of each series.

The First Preference Shares of each series rank equally with respect to the payment of dividends and the distribution of assets or return of capital in the event of liquidation, dissolution or winding-up and in priority to the Common Shares and any other shares of the Company ranking junior to the First Preference Shares. In addition, if any amount of cumulative dividend or declared non-cumulative dividend or an amount payable on return of capital in respect of shares of a series of First Preference Shares is not paid in full, the shares of the series are entitled to participate rateably with the shares of any other series of the same class in respect of such amounts.

In accordance with the provisions of the CBCA, the amendment of certain rights attaching to a class of shares, including Common Shares, requires the approval of not less than two-thirds of the votes cast by the holders of such shares voting at a special meeting of such holders. Pursuant to the Company's By-laws, a quorum for a meeting of the holders of Common Shares occurs when persons not being less than two in number and holding or representing by proxy not less than 33⅓% of the issued and outstanding Common Shares entitled to vote at such meetings are present, unless a higher number is designated by the Board. In circumstances where the rights of Commons Shares may be amended, to add, change or remove any provisions restricting or constraining the issue, transfer or ownership of Common Shares, holders of Common Shares have the right under the CBCA to dissent from such amendment and require the Company to pay them the then fair value of the Common Shares.

## **Shareholder Meetings**

There are two types of shareholder meetings: regular annual meetings and special meetings. Pursuant to the CBCA, the annual shareholder meeting shall be held not later than fifteen months after the holding of the last preceding annual meeting but no later than six months after the end of preceding financial year, unless an order extending the time for calling the annual meeting is obtained. The Directors may at any time call a special meeting of shareholders.

A notice stating the day, hour and place of meeting and, if special business is to be transacted details of the nature of the business, must be served by sending such notice to each person who is entitled to notice of such meeting and who on the record date for notice appears on the records of the Company or the Company's transfer agent as a shareholder entitled to vote at the meeting and to each director of the Company and to the auditor of the Company by prepaid mail not less than 21 days and not more than 60 days before the meeting unless such requirement is otherwise waived. The Company must fix a record date in advance of the meeting for the purpose of determining shareholders entitled to notice of the meeting. Only shareholders of record on such date will be entitled to notice of the meeting.

Votes at meetings of shareholders may be given either personally or by proxy. Every shareholder, including a shareholder that is a body corporate, entitled to vote at a meeting of shareholders may by means of a proxy appoint

a proxyholder or one or more alternate proxyholders, who need not be shareholders, as his nominee to attend and act at the meeting in the manner, to the extent and with the authority conferred by the proxy.

### **C. Material Contracts**

Except for contracts entered into in the ordinary course of business, the only material contract entered into by NovAtel in the two years immediately preceding the date of this Annual Report which can reasonably be regarded as presently material is the following:

- (1) Change of Control Agreement dated April 5, 2004 among NovAtel, Leica Geosystems and CMC Electronics, as more particularly described under "Item 4 — Information on the Company, Business Overview — Certain Contractual Rights."

### **D. Exchange Controls**

#### *Investment Canada Act*

Canada has no system of exchange controls. There is no law, government decree or regulation in Canada restricting the export or import of capital or affecting the remittance of dividends, interest or other payments to a non-resident holder of Common Shares, other than withholding tax requirements. See "Item 10 — Additional Information, Taxation."

There is no limitation imposed by Canadian law or by the articles or other charter documents of the Company or the right of a non-resident to hold or vote Common Shares or Preferred Shares of the Company with voting rights (collectively, "Voting Shares"), other than as provided in the Investment Canada Act (the "Investment Act"), as amended by the World Trade Organization Agreement Implementation Act (the "WTOA Act"). The Investment Act generally prohibits implementation of a reviewable investment by an individual, government or agency thereof, corporation, partnership, trust or joint venture that is not a "Canadian," as defined in the Investment Act (a "non-Canadian"), unless, after review, the minister responsible for the Investment Act is satisfied that the investment is likely to be of net benefit to Canada. An investment in Voting Shares of the Company by a non-Canadian (other than a "WTO Investor," as defined below) would be reviewable under the Investment Act if it was an investment to acquire control of the Company and the Company was not, immediately prior to the implementation of the investment, controlled by a WTO Investor, and the value of the assets of the Company were \$5.0 million or more. An investment in Voting Shares of the Company by a WTO Investor would be reviewable under the Investment Act if it was an investment to acquire direct control of the Company, and the value of the assets of the Company equaled or exceeded \$223 million for the year 2003 and \$237 million, the expected threshold, for the year 2004. A non-Canadian, whether a WTO Investor or otherwise, would acquire control of the Company for purposes of the Investment Act if he or she acquired a majority of the Voting Shares of the Company. The acquisition of less than a majority, but at least one-third of the Voting Shares of the Company, would be presumed to be an acquisition of control of the Company, unless it could be established that the Company was not controlled in fact by the acquirer through the ownership of Voting Shares. In general, an individual is a WTO Investor if he or she is a "national" of a country (other than Canada) that is a member of the World Trade Organization ("WTO Member") or has a right of permanent residence in a WTO Member other than Canada. A corporation or other entity will be a WTO investor if it is a "WTO investor-controlled entity" pursuant to detailed rules set out in the Investment Act. The United States is a WTO Member.

Certain transactions involving Voting Shares of the Company would be exempt from the Investment Act, including: (a) an acquisition of Voting Shares of the Company if the acquisition was made in connection with the person's business as a trader or dealer in securities; (b) an acquisition of control of the Company in connection with the realization of a security interest granted for a loan or other financial assistance and not for any purpose related to the provisions of the Investment Act; and (c) an acquisition of control of the Company by reason of an amalgamation, merger, consolidation or corporate reorganization, following which the ultimate direct or indirect control in fact of the Company, through the ownership of voting interests, remains unchanged.

## **E. Taxation**

The following is a summary of the principal Canadian federal income tax considerations generally applicable to a holder of Shares who is neither resident nor deemed to be resident in Canada, who does not use or hold and is not deemed to use or hold their Shares in carrying on a business in Canada and whose Shares do not otherwise constitute “taxable Canadian property” for purposes of the Tax Act (a “U.S. Holder”). Shares of a holder will generally not constitute “taxable Canadian property” unless (a) at any time within the sixty (60) months immediately preceding the disposition of Shares by such holder, such holder, persons not dealing at arm’s length with such holder, or any combination thereof, owned (or had options to acquire) 25% or more of the issued shares of any class or series of the capital stock of the Company or a predecessor, (b) a holder, upon ceasing to be a Canadian resident, elected under the Tax Act to have the Shares deemed to be taxable Canadian property, or (c) the Shares were acquired in circumstances under which they are deemed to be taxable Canadian property. The Tax Act contains provisions relevant to a non-resident insurer for whom any Securities are “designated insurance property” which this summary does not take into account. This summary is not exhaustive of all potential Canadian income tax consequences to a U.S. Holder of acquiring, holding or disposing of Common Shares.

This summary takes into account the current provisions of Tax Act, the regulations thereunder, all specific proposals to amend the Tax Act publicly announced prior to the date of this Annual Report, and the current published administrative practices and policies of the Canada Revenue Agency. It assumes that all proposals to amend the Tax Act will be enacted in their present form and otherwise does not take into account or anticipate changes in the law, whether by way of judicial decision or legislative action nor does it take into account provincial, territorial or foreign tax legislation or considerations.

A U.S. Holder will not be subject to tax under the Tax Act on any gain realized in respect of the disposition or deemed disposition of Common Shares to a person other than the Company. A disposition of the Shares to the Company may give rise to a deemed dividend that would be subject to Canadian withholding tax. Generally, dividends paid or credited, or deemed to be paid or credited by the Company are subject to Canadian withholding tax at the rate of 15% (reduced from 25% by the Convention) for U.S. Holders who beneficially own the dividends. The Company assumes responsibility for the withholding of tax on dividends to a U.S. Holder at the source.

## **F. Dividends and Paying Agents**

Not applicable.

## **G. Statement by Experts**

Not applicable.

## **H. Documents on Display**

Documents concerning the Company referred to in this Annual Report may be inspected at its headquarters at 1120–68<sup>th</sup> Avenue N.E., Calgary, Alberta, T2E 8S5, CANADA. The Company provides access to its Quarterly Reports filed on Form 6-K and Annual Report on Form 20-F on its website free of charge, as soon as reasonably practicable after those reports are electronically filed. The Company’s Code of Ethics and Business Conduct is posted on its website at [www.novatel.ca](http://www.novatel.ca).

The Company’s SEC filings and the exhibits thereto, are available for inspection and copying at the public reference facilities maintained by the SEC, 100 F Street N.E., Washington, D.C., 20549. Copies of these filings may be obtained from these offices after the payment of prescribed fees. Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms.

As a foreign private issuer, the Company is exempt from the proxy rules under the Securities Exchange Act of 1934, as amended, prescribing the furnishing and content of proxy statements to shareholders. As the Company

is a foreign private issuer, the Company's directors and officers are also exempt from the shortswing profit recovery and disclosure regime of Section 16 of the Exchange Act.

#### **I. Subsidiary Information**

Not applicable.

#### **Item 11. Quantitative and Qualitative Disclosures about Market Risk**

See "Item 5 — Operating and Financial Review and Prospects, Operating Results — Financial Instruments." The Company is not subject to significant interest rate risk due to the short-term maturities of the Company's outstanding loans and short-term investments.

#### **Item 12. Description of Securities other than Equity Securities**

Not applicable.

### **PART II**

#### **Item 13. Defaults, Dividend Arrearages and Delinquencies**

Not applicable.

#### **Item 14. Material Modifications to the Rights of Security Holders and Use of Proceeds**

Not applicable.

#### **Item 15. Controls and Procedures**

*Evaluation of Disclosure Controls and Procedures.* The Company's Chief Executive Officer and Chief Financial Officer, after evaluating the effectiveness of the Company's "disclosure controls and procedures" (as defined in the Securities Exchange Act of 1934, Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this Annual Report, have concluded that the Company's disclosure controls and procedures were effective.

*Changes in Internal Controls.* There were no changes in the Company's internal controls over financial reporting identified in connection with the evaluation above during the period covered by this Annual Report that has materially affected, or is reasonably likely to materially affect, the Company's internal controls over financial reporting.

#### **Item 16A. Audit Committee Financial Expert**

The Company's board of directors has determined that Joel A. Schleicher is the Company's audit committee financial expert as defined by the rules of the SEC. Mr. Schleicher is "independent" as defined by the NASD rules.

#### **Item 16B. Code of Ethics**

The Company has adopted a Code of Ethics and Business Conduct that applies to its principal executive officer, principal financial officer and all other officers, employees and directors of the Company. A copy of the Company's Code of Ethics and Business Conduct can be found on the Company's website at [www.novatel.ca](http://www.novatel.ca). There were no amendments to, or waivers granted under, the Code of Ethics and Business Conduct during the year ended December 31, 2005.

**Item 16C. Principal Accountant Fees and Services**

The following table sets forth the aggregate fees billed to the Company for the years ended December 31, 2005 and December 31, 2004:

<u>Fees</u>	<u>2005</u>	<u>2004</u>
Audit Fees (1) .....	\$306,058	\$361,095
Audit-Related Fees (2) .....	36,570	—
Tax Fees (3) .....	91,242	34,012
Other Fees (4) .....	—	—
<b>Total Fees</b> .....	<u><u>\$433,870</u></u>	<u><u>\$395,107</u></u>

- (1) Audit Fees “consist of fees billed for professional services rendered in connection with the audit of the Company’s consolidated annual financial statements, review of the Company’s quarterly financial statements and the quarterly and annual regulatory filings thereon. In 2004, includes \$159,530 related to a proposed Canadian public offering of the Company’s shares in May 2004.
- (2) “Audit-Related Fees” consist of fees for professional services rendered in connection with financial accounting and reporting consultations.
- (3) “Tax Fees” consist of fees billed for professional services rendered for tax compliance and tax advice. These services include preparation of the Company’s income tax returns, employee-related tax issues and excise tax matters.
- (4) “Other Fees” consist of fees for products and services other than the services reported above.

Effective February 13, 2003, the Audit Committee requires pre-approval of all audit and permissible non-audit services (including the fees and terms thereof) to be performed for the Company by its independent registered chartered accountants, subject to the de-minimis exception for non-audit services described in Section 10A(i)(1)(B) of the Securities Exchange act of 1934.

The Audit Committee reviews all non-audit related services provided by the independent registered chartered accountants to the Company, at each quarterly meeting. In 2005, the Audit Committee approved 100% of the non-audit related services provided in 2005.

**Item 16D. Exemptions from the Listing Standards for Audit Committees**

Not applicable.

**Item 16E. Purchases of Equity Securities by the Issuer and Affiliated Purchases**

The Company did not purchase any of its equity securities in 2004.

**Item 17. Financial Statements**

Not applicable.

**Item 18. Financial Statements**

See Item 19 below for Financial Statements filed as a part of this Annual Report.

## Item 19. Financial Statements and Exhibits

### (a) Financial Statements

1. Report of Independent Registered Chartered Accountants
2. Consolidated Balance Sheets
3. Consolidated Statements of Operations
4. Consolidated Statements of Shareholders' Equity
5. Consolidated Statements of Cash Flows
6. Notes to Consolidated Financial Statements
7. Financial Statement Schedules

### (b) Exhibits

Exhibit Number	Exhibit
3.1	Restated Articles of Incorporation of Registrant. (1)
3.2	Restated Bylaws of Registrant. (7)
4.1	Form of Common Stock Certificate. (1)
10.1	Directors Stock Option Plan.
10.2	Employee Stock Option Plan with form of stock option agreement.
10.3	Form of Indemnification Agreement to be entered into between Registrant and certain directors and officers. (1)
10.4	Employment Agreement dated July 1, 1997 between NovAtel Inc. and Werner Gartner. (3)
10.5	Lease Agreement (Building) dated January 29, 1999 between Christian Schumacher and NovAtel Inc. (2)
10.6	Agreement made effective July 20, 1999 between NovAtel Inc. and Sokkia Co., Ltd. (4)
10.7	License Agreement made effective August 1, 1999 between NovAtel Inc., Sokkia Co., Ltd. and Point, Inc. (4)
10.8	Operating Loan Credit Facility Letter from HSBC Bank Canada made effective November 6, 2000. (5)
10.9	Amendment made effective January 26, 2001 to Operating Loan Credit Facility Letter from HSBC Bank Canada. (5)
10.10	Employment Agreement dated April 5, 2004 between NovAtel Inc. and Jonathan W. Ladd. (7)
10.11	Operating Line of Credit Facility Letter from The Toronto Dominion Bank dated June 5, 2002. (6)
10.12	Employment Agreement dated November 20, 1996 between NovAtel Inc. and Patrick C. Fenton. (7)
* 10.13	Change of Control Agreement dated April 5, 2004 between NovAtel Inc. and Leica Geosystems A.G., CMC Electronics Inc., and Oncap L.P. (7)
10.14	2004 Employee Long-term Incentive Plan. (8)
21.1	List of Subsidiaries.
23.1	Consent of Deloitte & Touche LLP, Independent Registered Chartered Accountants.
31.1	Section 302 Certification of Chief Executive Officer.
31.2	Section 302 Certification of Chief Financial Officer.
32.1	Section 906 Certification of Chief Executive Officer.
32.2	Section 906 Certification of Chief Financial Officer.

(1) Incorporated by reference to Registrant's registration statement on Form F-1 (Registration Statement No. 333-6088).

(2) Incorporated by reference to Registrant's annual report on Form 20-F for the year ended December 31, 1998.

(3) Incorporated by reference to Registrant's annual report on Form 20-F for the year ended December 31, 1997.

(4) Incorporated by reference to Registrant's annual report on Form 20-F for the year ended December 31, 1999.



- (5) Incorporated by reference to Registrant's annual report on Form 20-F for the year ended December 31, 2000.
- (6) Incorporated by reference to Registrant's annual report on Form 20-F for the year ended December 31, 2002.
- (7) Incorporated by reference to Registrant's annual report on Form 20-F for the year ended December 31, 2003.
- (8) Incorporated by reference to Registrant's annual report on Form 20-F for the year ended December 31, 2004.

\* Certain portions of this agreement have been omitted and filed separately with the Securities and Exchange Commission. Confidential treatment has been granted with respect to the omitted portions.

Copies of the Company's SEC filings and the above exhibits are available for inspection and copying at the public reference facilities maintained by the SEC, 100 F Street N.E., Washington, D.C., 20549 or through the SEC's website at [www.sec.gov](http://www.sec.gov). You may also request copies of the above exhibits by contacting our investor relations department by telephone (403-295-4532) or by e-mail ([ir@novatel.com](mailto:ir@novatel.com)).

## SIGNATURES

The Registrant hereby certifies that it meets all of the requirements for filing on Form 20-F/A and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

NOVATEL INC.

By: /s/ Jonathan W. Ladd  
Jonathan W. Ladd  
*President and Chief Executive Officer*

Date: May 24, 2006

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**NOVATEL INC.**

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## MANAGEMENT'S REPORT

Management is responsible to the Board of Directors for the preparation of the Company's consolidated financial statements. These statements have been prepared in accordance with generally accepted accounting principles in Canada and necessarily include certain amounts based on estimates and judgments. Management has determined such amounts on a reasonable basis to ensure that the consolidated financial statements are presented fairly, in all material respects. Financial information presented elsewhere in this Annual Report is consistent with that in the consolidated financial statements.

The Company maintains a system of internal controls which provides management with reasonable assurance that assets are safeguarded and that reliable financial records are maintained.

The external auditors, Deloitte & Touche LLP, have been appointed by the shareholders to express an opinion as to whether these consolidated financial statements present fairly the Company's consolidated financial position and operating results in accordance with generally accepted accounting principles in Canada. Their report follows.

The Board of Directors has reviewed and approved these consolidated financial statements. To assist the Board in meeting its responsibility, it has appointed an Audit Committee, all of whose members are outside directors. The committee meets periodically with management and the external auditors to review internal controls, audit results and accounting principles and practices. The external auditors have full and free access to the Audit Committee.

/s/ Jonathan W. Ladd

Jonathan W. Ladd

President and Chief Executive Officer

/s/ Werner Gartner

Werner Gartner

Executive Vice President and Chief Financial Officer

February 9, 2006

## **REPORT OF INDEPENDENT REGISTERED CHARTERED ACCOUNTANTS**

**To the Board of Directors and Shareholders of NovAtel Inc.,**

We have audited the consolidated balance sheets of NovAtel Inc. as at December 31, 2005 and 2004, and the consolidated statements of operations, shareholders' equity and cash flows for each of the years in the three year period ended December 31, 2005. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards and the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of NovAtel Inc. as at December 31, 2005 and 2004 and the results of its operations and its cash flows for each of the years in the three year period ended December 31, 2005 in accordance with Canadian generally accepted accounting principles.

The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly we express no such opinion.

(signed) "Deloitte & Touche LLP"

Deloitte & Touche LLP  
Independent Registered Chartered Accountants  
Calgary, Alberta, Canada  
February 9, 2006

### **COMMENTS BY INDEPENDENT REGISTERED CHARTERED ACCOUNTANTS FOR U.S. READERS ON CANADA-U.S. REPORTING DIFFERENCES**

The standards of the Public Company Accounting Oversight Board (United States) require the addition of an explanatory paragraph (following the opinion paragraph) when there are changes in accounting principles that have a material effect on the comparability of the Company's financial statements or changes that have been implemented in the financial statements such as those described in Note 2 to the consolidated financial statements. Our report to the board of directors and shareholders on the consolidated financial statements of NovAtel Inc., dated February 9, 2006, is expressed in accordance with Canadian reporting standards which do not require a reference to such changes in accounting principles in the auditors' report when the change is properly accounted for and adequately disclosed in the financial statements.

(signed) "Deloitte & Touche LLP"

Deloitte & Touche LLP  
Independent Registered Chartered Accountants  
Calgary, Alberta, Canada  
February 9, 2006

NOVATEL INC.

CONSOLIDATED BALANCE SHEETS

(in thousands, Canadian dollars)

	December 31,	
	2005	2004
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents (Note 8) (includes \$nil compensating balances at December 31, 2005 and \$1,000 at December 31, 2004) .....	\$ 2,721	\$ 8,949
Short-term investments (Note 8) (includes compensating balances of \$4,158 at December 31, 2005 and \$3,158 at December 31, 2004) .....	32,363	14,410
Accounts receivable (Notes 3 and 12) .....	10,694	9,413
Related party receivables (Note 16) .....	1,331	1,591
Related party notes receivable (Note 16) .....	1,552	1,614
Inventories (Note 4) .....	5,436	5,191
Prepaid expenses and deposits .....	599	268
Future income tax asset — current portion (Note 15) .....	2,370	1,286
Total current assets .....	57,066	42,722
Capital assets (Note 5) .....	3,095	3,447
Intangible assets (Notes 6 and 9) .....	4,722	2,515
Goodwill (Note 20) .....	1,494	—
Deferred development costs (Note 7) .....	1,657	2,359
Future income tax asset — long term portion (Note 15) .....	3,221	1,903
Total assets .....	<u>\$71,255</u>	<u>\$52,946</u>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable and accrued liabilities .....	\$ 9,784	\$ 9,148
Related party payables (Note 16) .....	15	345
Notes payable (Note 17) .....	1,552	1,614
Deferred revenue and customer deposits .....	752	755
Provision for future warranty costs .....	693	538
Total current liabilities .....	12,796	12,400
Deferred gain on sale/leaseback of capital assets (Note 5) .....	342	453
Total liabilities .....	<u>13,138</u>	<u>12,853</u>
Commitments, contingencies and guarantees (Note 9)		
Shareholders' equity (Note 11):		
Capital stock .....	39,667	38,870
(Common shares issued and outstanding: 8,365 at December 31, 2005 and 8,260 at December 31, 2004)		
Contributed surplus .....	953	442
Retained earnings .....	17,497	781
Total shareholders' equity .....	<u>58,117</u>	<u>40,093</u>
Total liabilities and shareholders' equity .....	<u>\$71,255</u>	<u>\$52,946</u>

*The accompanying notes are an integral part of these consolidated financial statements.*

NOVATEL INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data, Canadian dollars)

	Year Ended December 31		
	2005	2004	2003
Revenues (Notes 12 and 16)			
Product sales .....	\$59,306	\$48,802	\$32,138
NRE fees .....	3,989	5,130	6,546
Total revenues .....	<u>63,295</u>	<u>53,932</u>	<u>38,684</u>
Cost of sales (Note 16) .....			
Cost of product sales .....	22,323	19,586	14,805
Cost of NRE fees .....	2,313	2,917	3,565
Total cost of sales .....	<u>24,636</u>	<u>22,503</u>	<u>18,370</u>
Gross profit .....	38,659	31,429	20,314
Operating expenses:			
Research and development .....	10,882	9,588	7,123
Selling and marketing .....	6,387	5,751	5,269
General and administration .....	7,082	5,312	4,280
Foreign exchange loss .....	255	595	527
Share offering costs (Note 13) .....	—	754	—
Total operating expenses .....	<u>24,606</u>	<u>22,000</u>	<u>17,199</u>
Operating income .....	14,053	9,429	3,115
Interest income, net .....	787	313	174
Other expense (Note 14) .....	(72)	(67)	(137)
Benefit of investment tax credits .....	1,592	4,356	—
Income from continuing operations before income taxes .....	16,360	14,031	3,152
Income taxes (Note 15)			
Current provision .....	2,046	2,328	52
Future income tax expense (benefit) .....	(2,402)	(1,091)	—
Total income tax expense (benefit) .....	(356)	1,237	52
Net income from continuing operations .....	16,716	12,794	3,100
Income from discontinued operations (Note 18) .....	—	21	360
Net income .....	<u>\$16,716</u>	<u>\$12,815</u>	<u>\$ 3,460</u>
Net income per share (basic) (Note 11)			
Continuing operations .....	\$ 2.01	\$ 1.59	\$ 0.40
Discontinued operations .....	—	—	0.05
Net income per share (basic) .....	<u>\$ 2.01</u>	<u>\$ 1.59</u>	<u>\$ 0.45</u>
Weighted average shares outstanding (basic) (Note 11) .....	<u>8,298</u>	<u>8,063</u>	<u>7,723</u>
Net income per share (diluted) (Note 11)			
Continuing operations .....	\$ 1.91	\$ 1.51	\$ 0.39
Discontinued operations .....	—	—	0.04
Net income per share (diluted) .....	<u>\$ 1.91</u>	<u>\$ 1.51</u>	<u>\$ 0.43</u>
Weighted average shares outstanding (diluted) (Note 11) .....	<u>8,763</u>	<u>8,500</u>	<u>7,983</u>

The accompanying notes are an integral part of these consolidated financial statements.



NOVATEL INC.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(in thousands, Canadian dollars)

	Common Shares (Note 11)		Contributed Surplus	Retained Earnings (Deficit)	Total Shareholders' Equity
	Number	Amount			
January 1, 2003 .....	7,685	\$35,572	\$ 13	\$(15,038)	\$20,547
Common shares issued pursuant to exercise of stock options (Note 11) .....	301	1,449	—	—	1,449
Repurchase of shares .....	(2)	(9)	—	—	(9)
Net income .....	—	—	—	3,460	3,460
December 31, 2003 .....	<u>7,984</u>	<u>\$37,012</u>	<u>\$ 13</u>	<u>\$(11,578)</u>	<u>\$25,447</u>
Change in accounting policy relating to stock-based compensation (Note 2(i)) .....	—	66	390	(456)	—
Common shares issued pursuant to exercise of stock options (Note 11) .....	276	1,792	(287)	—	1,505
Stock based compensation .....	—	—	326	—	326
Net income .....	—	—	—	12,815	12,815
December 31, 2004 .....	<u>8,260</u>	<u>\$38,870</u>	<u>\$ 442</u>	<u>\$ 781</u>	<u>\$40,093</u>
Common shares issued pursuant to exercise of stock options Note 11) .....	105	797	(76)	—	721
Stock based compensation .....	—	—	587	—	587
Net income .....	—	—	—	16,716	16,716
December 31, 2005 .....	<u>8,365</u>	<u>\$39,667</u>	<u>\$ 953</u>	<u>\$ 17,497</u>	<u>\$58,117</u>

*The accompanying notes are an integral part of these consolidated financial statements.*

NOVATEL INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands of Canadian dollars)

	Year Ended December 31		
	2005	2004	2003
Operating activities:			
Net income .....	\$ 16,716	\$ 12,815	\$ 3,460
Share offering costs (Note 13) .....	—	754	—
Charges and credits to operations not involving an outlay of cash:			
Amortization .....	2,921	2,390	1,807
Loss (gain) on disposal of capital assets .....	19	19	(66)
Current income tax provision and future income tax benefit .....	(440)	1,167	—
Benefit of investment tax credits .....	(1,592)	(4,356)	—
Gain on liquidation of Mezure assets and liabilities (Note 18) .....	—	(21)	(379)
Stock based compensation expense .....	587	326	—
Amortization of deferred gain on sale/leaseback of capital assets .....	(111)	(114)	(118)
Accretion on royalty payable to CMC related to GPS OEM product line acquisition .....	17	54	37
Net change in non-cash working capital related to operations (Note 21) ..	(1,025)	(530)	3,272
Cash provided by operating activities .....	<u>17,092</u>	<u>12,504</u>	<u>8,013</u>
Financing activities:			
Issuance of shares (Note 11) .....	721	1,505	1,449
Repurchase of shares (Note 11) .....	—	—	(9)
Related party notes receivable .....	55	(11)	(140)
Notes payable .....	(55)	11	172
Receipts (payments) related to share offering costs (Note 13) .....	57	(807)	—
Payment of capital lease obligations .....	—	(100)	(90)
Effect of exchange rate changes on financing activities .....	—	—	(74)
Cash provided by financing activities .....	<u>778</u>	<u>598</u>	<u>1,308</u>
Investing activities:			
Purchase of capital and intangible assets .....	(2,446)	(2,293)	(2,656)
Proceeds from disposal of capital assets .....	53	29	157
Purchase of short-term investments .....	(56,350)	(17,720)	(16,971)
Proceeds from short-term investments .....	38,397	13,865	11,288
Acquisition of Waypoint Consulting Inc. (Note 20) .....	(3,531)	—	—
Acquisition of CMC Electronics' OEM GPS business (Note 19) .....	—	—	(155)
Royalty payment relating to CMC Electronics' OEM GPS business (Note 19) .....	(221)	(261)	(82)
Deferred development costs .....	—	(218)	(157)
Cash used in investing activities .....	<u>(24,098)</u>	<u>(6,598)</u>	<u>(8,576)</u>
(Decrease) increase in cash and cash equivalents .....	(6,228)	6,504	745
Cash and cash equivalents beginning of year .....	<u>8,949</u>	<u>2,445</u>	<u>1,700</u>
Cash and cash equivalents, end of year .....	<u>\$ 2,721</u>	<u>\$ 8,949</u>	<u>\$ 2,445</u>
Interest paid related to bank advances and capital lease obligations .....	—	\$ 3	\$ 10
Income taxes paid .....	<u>\$ 91</u>	<u>\$ 71</u>	<u>\$ 83</u>

The accompanying notes are an integral part of these consolidated financial statements.

## Notes to consolidated financial statements

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

### NOTE 1 NATURE OF BUSINESS

NovAtel Inc. ("NovAtel" or the "Company") is incorporated under the laws of Canada. The Company designs, markets and supports a broad range of products that determine precise geographic locations using the Global Positioning System ("GPS") and other positioning technologies.

On July 20, 1999, the Company and Sokkia Co., Ltd. formed a joint venture, Point, Inc. to develop and distribute GPS based products for surveying, mapping, geographical information systems, construction and construction machine control applications, on a world-wide basis (see Note 17).

On April 17, 1998, CMC Electronics Inc. ("CMC Electronics"), formerly BAE SYSTEMS CANADA INC., acquired 58.3% of the Company's outstanding common shares from the Company's two former principal shareholders (see Note 15).

On April 11, 2001, an investor group led by ONCAP L.P. ("ONCAP") acquired control of the Company through the acquisition of CMC Electronics (see Note 15). From January 2005 through August 2005, CMC Electronics sold approximately 4.5 million common shares through open market transactions, reducing its ownership of the Company from approximately 55% to 0%.

As of December 31, 2005, the Company owned a 70% equity interest in Mezure, Inc., a company that had been developing a GPS, wireless communication and Internet-based product for deformation monitoring of manmade and natural structures. On April 8, 2003, the shareholders of Mezure voted unanimously to proceed with a Chapter 7 bankruptcy filing for Mezure, which was concluded on September 24, 2003. Consequently, the Company treated Mezure as a discontinued operation for all periods presented (see Note 18).

On October 1, 2005 the Company acquired Waypoint Consulting Inc. ("Waypoint") for approximately \$3.5 million in cash, subject to post-closing adjustments to working capital. Waypoint's products include specialized real-time and post-processing GPS and GPS/inertial positioning and trajectory software (see Note 20).

### NOTE 2 SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared by management in accordance with generally accepted accounting principles in Canada and are stated in Canadian dollars. The material differences between Canadian and United States (U.S.) generally accepted accounting principles are described in Note 23. The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the reporting period. Actual results could differ from those estimated.

#### a) *Principles of Consolidation*

The consolidated financial statements include the accounts of the Company, its continuing subsidiaries and its proportionate 49% joint venture interest in Point, Inc.

#### b) *Foreign Currency Translation*

Foreign subsidiaries and Point, Inc. are considered financially and operationally dependent on the Company and are translated into Canadian dollars using current rates of exchange for monetary assets

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

and liabilities, historical rates of exchange for non-monetary assets and liabilities, and average rates for the period for revenues and expenses, except amortization and cost of sales, which are translated at the rate of exchange applicable to the related assets. Gains and losses resulting from these translation adjustments are included in operating income.

Transactions and monetary balances denominated in a currency other than the Canadian dollar are translated into Canadian dollars using yearly average and year-end exchange rates, respectively. Gains and losses arising from this translation process are included in operating income.

### c) *Cash and Cash Equivalents, Short Term Investments*

Cash and cash equivalents include highly liquid investments which have original maturities of 90 days or less. Short-term investments include highly liquid investments which have original maturities of 91 days to 12 months.

### d) *Inventories*

Raw materials and components, work-in-progress, and finished goods inventories are recorded at the lower of cost or net realizable value. Cost is determined on a first-in, first-out basis and includes materials, labour and manufacturing overhead.

### e) *Capital Assets, Intangible Assets and Amortization*

Capital assets are recorded at cost. Maintenance and repair costs of a routine nature are charged to operations as incurred, and renewals and betterments that extend the economic useful life of an asset are capitalized.

Capital assets and intangible assets are amortized on a straight-line basis using the expected useful lives of the assets:

Computer and ancillary equipment .....	4 years
Research and development equipment .....	4 years
Production equipment .....	5 years
Automobiles .....	5 years
Leasehold improvements .....	Shorter of useful life or the term of leases
Furniture and fixtures .....	10 years
Product tooling .....	2-4 years
Patents and trademarks .....	10 years
Technology .....	4-10 years
Software licenses .....	4 years
Market presence of CMC Electronics OEM GPS and Waypoint product lines .....	4-8.5 years

Capital assets and intangible assets are assessed for future recoverability or impairment by estimating future net undiscounted cash flows and residual values. When impairment has occurred, a loss is recognized in the period. When the carrying value of a long-lived asset is greater than its net recoverable amount as determined on an estimated undiscounted cash flow basis, an impairment loss is recognized to the extent that its fair value, measured as the discounted cash flows over the life of the asset when quoted market prices are not readily available, is below the asset's carrying value.

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

### f) *Revenue Recognition*

The Company recognizes product revenue when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable and collectibility is reasonably assured. Revenues from non-recurring engineering ("NRE") fees are recognized at the time services are rendered. On long-term contracts, in which the customer pays established rates for time and materials, revenue is recognized as services are rendered and costs are incurred. On certain long-term contracts, revenue is recognized using the proportional performance method relative to customer milestones achieved. Revisions in cost and profit estimates during the course of work are reflected in the period in which the need for revision becomes known. Losses, if any, are recognized fully when first anticipated. Some contracts contain penalty provisions based on performance relative to established targets. Such penalties are included in revenue or cost estimates when amounts can be reasonably determined.

The Company applies U.S. Statement of Position 97-2, *Software Revenue Recognition*, to product sales where software is considered more than incidental. For software arrangements involving multiple elements, the Company allocates revenue to each element based on the relative fair value or the residual method, as applicable, and using vendor specific objective evidence of fair values, which is based on prices charged when the element is sold separately. Software revenue is recognized when persuasive evidence of an arrangement exists, the software is delivered in accordance with all terms and conditions of the customer contracts, the fee is fixed or determinable and collection is reasonably assured. Revenue related to post-contract support ("PCS"), including technical support and unspecified when-and-if available software upgrades, is recognized ratably over the PCS term.

### g) *Research and Development Costs*

Research costs are charged to operations as incurred. Development costs, including software development costs, are charged to operations as incurred unless they meet specific criteria related to technical, market and financial feasibility. In these circumstances, the costs are deferred and amortized on a systematic basis, using a method similar to the unit-of-production method of amortization, subject to an estimate of recoverability.

### h) *Provision for Future Warranty Costs*

Warranty costs are accrued, to the extent that they are not recoverable from third party manufacturers, for the estimated cost to repair products for the balance of the warranty periods.

### i) *Stock-based Compensation Plans*

The Company has stock-based compensation plans (see Note 11). Effective January 1, 2004, the Company adopted the fair value method of accounting for stock options awarded to employees on or after January 1, 2002 as required by amended CICA Handbook Section 3870 *Stock-Based Compensation and Other Stock-Based Payments*. As permitted by the transitional provisions of Section 3870, the change was adopted retroactively without restatement. Under Section 3870, the fair value of stock options is recognized over the applicable vesting period as stock-based compensation expense and a credit to contributed surplus. When options are exercised, the proceeds are credited to share capital, and the applicable fair value is reclassified from contributed surplus to share capital. Retroactive application of Section 3870 resulted in the January 1, 2004 opening balances of deficit, contributed surplus and share capital being increased by \$456, \$390 and \$66, respectively, as though the fair value method had been applied since January 1, 2002.

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

### j) *Hedging Relationships*

Effective January 1, 2004, the Company adopted Accounting Guideline 13, "Hedging Relationships." The guideline establishes conditions where hedge accounting may be applied. Where hedge accounting does not apply, any changes in the fair values of the financial contracts are taken into income in the period of change. The Company enters into forward foreign currency contracts to reduce its exposure to fluctuations in the exchange rates between the Canadian dollar and the U.S. dollar and Euro. These contracts qualify as hedges under the new accounting guideline and the Company applies hedge accounting to its financial instruments.

### k) *Impairment of Long-Lived Assets*

The Company reviews both long-lived assets to be held and used and identifiable intangible assets with finite lives whenever events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable. Determination of recoverability is based on an estimate of undiscounted future cash flows resulting from the use of the asset and its eventual disposition. Measurement of an impairment loss for long-lived assets and certain identifiable intangible assets that management expects to hold and use is based on the fair value of the assets, whereas such assets to be disposed of are reported at the lower of carrying amount or fair value less costs to sell. As at December 31, 2005, the company determined that there were no triggering events requiring impairment analysis.

Goodwill impairment is assessed at the reporting unit level at least annually, or more frequently if events or circumstances indicate there may be impairment. Potential impairment is identified when the carrying value of a reporting unit, including the allocated goodwill, exceeds its fair value. Goodwill impairment is measured as the excess of the carrying amount of the reporting unit's allocated goodwill over the implied fair value of the goodwill, based on the fair value of the assets and liabilities of the reporting unit. The fair values are estimated using accepted valuation methodologies such as discounted future net cash flows, earnings multiples or prices for similar assets, whichever is most appropriate under the circumstances.

### l) *Asset retirement obligations*

In December 2003, the CICA issued CICA Handbook Section 3110 "Asset Retirement Obligations" which requires the liability recognition for future retirement obligations associated with capital assets. These obligations are initially recognized at fair value, which is the discounted future value of the liability. This fair value is capitalized as part of the cost of the related capital asset and amortized over its useful life. The liability accretes until the Company settles the retirement obligation. The Company retroactively adopted this standard on January 1, 2004. The adoption of this new standard did not have a material impact on the Company's financial statements.

### m) *Variable Interest Entities*

Effective January 1, 2005, the Company adopted revised CICA Accounting Guideline 15 ("AcG-15"), "Consolidation of Variable Interest Entities". AcG-15 provides guidance for applying consolidation principles to certain entities (defined as VIEs) that are subject to control on a basis other than ownership of voting interests. An entity is a VIE when, by design, one or both of the following conditions exist: (a) total equity investment at risk is insufficient to permit that entity to finance its activities without additional subordinated support from other parties; (b) as a group, the holders of the equity investment at risk lack certain essential characteristics of a controlling financial interest. AcG-15 requires consolidation by a business of VIEs in which it is the primary beneficiary. The primary beneficiary is

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

defined as the party that has exposure to the majority of the expected losses and/or expected residual returns of the VIE. The adoption of this guideline did not have a material impact on the consolidated financial statements.

n) ***Income Taxes***

The Company follows the liability method of accounting for income taxes. Under this method, current income taxes are recognized for the estimated income taxes payable for the current year. Future income tax assets and liabilities are recognized for temporary differences between the tax and accounting bases of assets and liabilities as well as for the benefit of losses available to be carried forward to future years for tax purposes that are more likely than not to be realized. In establishing the appropriate income tax valuation allowances, the Company assesses the realizability of its net future income tax assets and based on all available evidence, both positive and negative, determines whether it is more likely than not that the remaining net future income tax assets or a portion thereof will be realized. (see Note 15).

o) ***Investment Tax Credits***

Investment tax credits relating to scientific research and development and capital expenditures are accounted for using the cost reduction method and are recognized once there is reasonable assurance that the Company will be able to realize the benefit from these credits.

p) ***Earnings Per Share***

Basic earnings per share is calculated by dividing the net earnings available to common shareholders by the weighted average number of common shares outstanding. Diluted earnings per share reflects the potential dilution that would occur if stock options were exercised. The treasury stock method is used in calculating diluted earnings per share, which assumes that any proceeds received from the exercise of in-the-money stock options, including those not currently exercisable, would be used to purchase common shares at the average market price for the period.

### NOTE 3 ACCOUNTS RECEIVABLE

	<u>December 31, 2005</u>	<u>December 31, 2004</u>
Trade receivables, net .....	\$ 9,840	\$8,909
Interest receivable .....	231	196
Goods and Services Tax receivable .....	218	164
Other .....	405	144
	<u>\$10,694</u>	<u>\$9,413</u>

The receivable balances are net of an allowance for doubtful accounts and sales returns of \$1,080 at December 31, 2005 and \$1,207 at December 31, 2004.

### NOTE 4 INVENTORIES

	<u>December 31, 2005</u>	<u>December 31, 2004</u>
Raw materials and components, net .....	\$2,378	\$2,174
Work-in-progress .....	552	345
Finished goods, net .....	<u>2,506</u>	<u>2,672</u>
	<u>\$5,436</u>	<u>\$5,191</u>

The inventory balances are net of a provision for excess and obsolete inventory of \$1,546 at December 31, 2005 and \$2,023 at December 31, 2004.

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

### NOTE 5 CAPITAL ASSETS

	December 31, 2005			December 31, 2004		
	Cost	Accumulated Amortization	Net	Cost	Accumulated Amortization	Net
Computer and ancillary equipment ...	\$ 2,797	\$1,689	\$1,108	\$ 3,875	\$2,837	\$1,038
Production, research and development equipment .....	4,105	3,021	1,084	3,740	2,608	1,132
Automobiles .....	26	9	17	26	3	23
Leasehold improvements .....	201	121	80	170	73	97
Furniture and fixtures .....	1,770	1,491	279	1,757	1,319	438
Product tooling .....	1,445	919	526	1,787	1,069	718
Equipment under capital lease .....	3	2	1	3	2	1
	<u>\$10,347</u>	<u>\$7,252</u>	<u>\$3,095</u>	<u>\$11,358</u>	<u>\$7,911</u>	<u>\$3,447</u>

On January 29, 1999, the Company concluded a sale/leaseback arrangement by which the Calgary facility, including certain adjacent land, with a carrying value of \$5,812 at time of sale, was sold for net proceeds of \$6,922, resulting in a gain of \$1,110. The gain on the sale of the facility has been deferred and is being amortized on a straight-line basis over the ten year term of the lease.

### NOTE 6 INTANGIBLE ASSETS

Intangible assets subject to amortization are as set out below:

	December 31, 2005			December 31, 2004		
	Cost	Accumulated Amortization	Net	Cost	Accumulated Amortization	Net
Patents and trademarks .....	\$ 4,262	\$2,860	\$1,402	\$3,925	\$2,450	\$1,475
Technology .....	3,670	2,254	1,416	2,410	2,173	237
Software licences .....	3,691	2,458	1,233	3,133	2,548	585
Market presence of CMC Electronics' OEM GPS and Waypoint's product lines .....	906	235	671	348	130	218
Total intangibles .....	<u>\$12,529</u>	<u>\$7,807</u>	<u>\$4,722</u>	<u>\$9,816</u>	<u>\$7,301</u>	<u>\$2,515</u>

For the years ended December 31, 2005, 2004 and 2003, amortization expense of intangibles was \$941 and \$757, and 564 respectively. The weighted-average amortization period is 6.9 years.

The estimated aggregate amortization expense for intangible assets for the five succeeding years is as follows:

2006 .....	\$1,128
2007 .....	900
2008 .....	738
2009 .....	561
2010 .....	547



## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

### NOTE 7 DEFERRED DEVELOPMENT COSTS

	<u>December 31, 2005</u>	<u>December 31, 2004</u>
Deferred development costs .....	\$ 2,900	\$3,064
Accumulated amortization .....	<u>(1,243)</u>	<u>(705)</u>
	<u>\$ 1,657</u>	<u>\$2,359</u>

The Company has deferred certain costs related to the development of a certified aviation GPS receiver. The Company amortizes these deferred costs using a method similar to the unit-of-production method of amortization. The following table discloses the development costs which have been deferred and the amortization of deferred development costs:

	<u>Year Ended December 31</u>		
	<u>2005</u>	<u>2004</u>	<u>2003</u>
Deferred development costs .....	\$ —	\$218	\$157
Amortization of deferred development costs .....	\$538	\$416	\$196

At December 31, 2005, the Company had deferred \$1,657 of development costs, net of accumulated amortization. The continued deferral of these costs is subject to recoverability based on estimates of future sales of the certified aviation GPS receiver. On April 5, 2004, the Company and CMC Electronics entered into a Strategic Cooperation Agreement which *inter alia* provides for certain guaranteed future payments over the following four years. Under the current business programs between the Company and CMC Electronics, the Company would expect these future guaranteed payments to substantially recover the \$1,657 of deferred development costs as of December 31, 2005. Should future actual or estimated sales of this receiver be materially lower than that currently estimated, a portion of the deferred development costs would be charged to results of operations.

### NOTE 8 BANK ADVANCES

At December 31, 2005, lines of credit were available with certain Canadian financial institutions. The lines of credit are payable on demand and are secured by \$4,158 of cash and short-term investments held as compensating balances. The credit line advances bear interest at the financial institutions' prime rate (December 31, 2005 — 5.0%) on Canadian dollar advances.

In aggregate, the Company can borrow up to \$1,650 for day-to-day operating requirements and \$3,350 to support the margin requirements related to the purchase of up to between U.S. \$ \$14,000 and \$15,000 of forward foreign exchange contracts (depending on the maturity date of the contracts). At December 31, 2005, portions of the lines of credit were utilized to support approximately U.S. \$ 8,500 of foreign exchange contracts (\$7,500 at December 31, 2004) leaving \$1,650 available for day-to-day operating requirements and the margin capacity available to enter into approximately U.S. \$5,500 to \$6,500 in forward foreign exchange contracts (depending on the maturity date of the contracts).

### NOTE 9 COMMITMENTS, CONTINGENCIES AND GUARANTEES

- a) At December 31, 2005, purchase commitments were outstanding for approximately \$11.5 million pertaining primarily to the acquisition of inventory, supplies and services in the normal course of business.

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

- b) The Company's facilities and certain equipment are leased for various periods up to 2016. Payments under the leasing arrangements are estimated to be as follows:

	<u>Operating Leases</u>
2006 .....	\$ 1,078
2007 .....	1,267
2008 .....	1,238
2009 .....	1,316
2010 .....	1,320
2011 and beyond .....	8,466
Total future minimum lease payments .....	<u>\$14,685</u>

The Company's rent expense associated with its facilities was \$883 in 2005, \$910 in 2004 and \$859 in 2003.

As of December 31, 2005, the landlord of the Company's Calgary facility was constructing an expansion of the facility at the request of and for the use of the Company. The construction is expected to be completed by mid 2006. As part of the arrangement with the landlord of the Calgary facility, the Company is responsible for approximately \$1.4 million of construction and leasehold improvement costs to be incurred in 2006. The Company expects its lease obligations for its existing facility and the expansion in Calgary to be approximately \$14 million over a ten year lease term, commencing with the completion of the construction expected in August 2006. These lease obligations have been included in the operating lease amounts disclosed above.

- c) As at December 31, 2005, intangible assets include unamortized costs of \$77 related to the Company's 1996 settlement agreement with Trimble Navigation Limited (Trimble). This settlement agreement with Trimble includes a provision that Trimble may, at its sole option, terminate rights granted thereunder, including licenses, should the Company undergo a direct change in control. On June 26, 2001, the Company received notice from Trimble terminating the licenses and rights under the settlement agreement in connection with the share acquisition by CMC Electronics in April 1998. The Company has sought legal advice regarding Trimble's termination rights under the 1996 settlement agreement and is continuing to evaluate the impact, if any, of Trimble's notice of termination. As this matter has not been resolved as of December 31, 2005, the Company has not provided for any impairment of these intangible assets. The Company does not expect this issue to materially affect the financial position, results of operations, or liquidity of the Company.
- d) The Company is subject to legal proceedings and other claims which arise in the ordinary course of its business. The Company has sought legal advice on these matters. In the opinion of management, the ultimate liability with respect to the resolution of these actions is not expected to materially affect the financial position, results of operations, or liquidity of the Company.
- e) In the normal course of operations, the Company provides indemnifications that are often standard contractual terms to counterparties in transactions such as purchase and sale contracts and service agreements. These indemnification agreements may require the Company to compensate the counterparties for costs incurred as a result of various events, changes in (or in the interpretation of) laws and regulations, or as a result of litigation claims or statutory sanctions that may be suffered by the counterparty as a consequence of the transaction. The terms of these indemnification agreements will vary based upon the contract, the nature of which prevents the Company from making a reasonable estimate of the maximum potential amount it could be required to pay counterparties. Historically, the Company

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

has not made any payments under such indemnifications and no amounts have been accrued in the accompanying consolidated financial statements.

### NOTE 10 FINANCIAL INSTRUMENTS

In the normal course of business, the Company uses forward foreign currency contracts to reduce its exposure to fluctuations in the exchange rates between the Canadian dollar and the U.S. dollar and the Euro. The Company documents the relationship between hedging instruments and hedged items, as well as its risk management objective for undertaking hedging transactions. The process includes linking hedging instruments to assets and liabilities on the balance sheet or to forecasted transactions. The Company also assesses, both at the hedge's inception and on an ongoing basis, whether the foreign currency contracts that are used in hedging transactions are effective in offsetting changes in fair values or cash flows of hedged items. The contracts are normally for terms of up to twelve months and are used as hedges of a portion of the Company's U.S. dollar and Euro denominated revenues. The contracts are not used for trading or speculative purposes. Foreign exchange gains and losses on foreign currency contracts used to hedge current foreign currency assets and liabilities are accrued under current assets or liabilities on the balance sheet and recognized currently in operating income, offsetting the respective translation gains and losses recognized on the underlying asset or liability.

Foreign exchange gains and losses on foreign currency contracts used to hedge anticipated U.S. dollar and Euro revenues beyond 60 days are applied against the underlying revenue when these revenues are recognized.

At December 31, 2005, the Company had forward currency contracts to sell U.S. \$ 8,000 between January 30, 2006 and August 31, 2006 at an average rate of \$0.8322 per Canadian dollar. In addition, the Company had forward foreign currency contracts to sell 320 Euro on February 28, 2006 at a rate of 0.6677 Euro per Canadian dollar.

The carrying values of other financial instruments, which include cash and cash equivalents, short-term investments, accounts receivable, related party receivables and advances, related party notes receivable, accounts payable and accrued liabilities, related party payables and notes payable approximate their fair value because of the near-term maturity of these instruments.

### NOTE 11 SHAREHOLDERS' EQUITY

The Company has authorized an unlimited number of common shares and first preference shares, of which 8,365 common shares are outstanding as of December 31, 2005 (8,260 in 2004 and 7,984 in 2003).

Net income (loss) per share figures presented in the Company's financial statements are based upon the weighted average number of shares outstanding. Diluted net income (loss) per share figures are computed as if the dilutive instruments were exercised at the beginning of the period (or the time of issuance, if later) and the funds obtained were used to purchase common shares at the average market price during the period.

The Company maintains stock option plans for employees and members of the Board of Directors. Under the plans, participants are granted options to purchase common shares at no less than the market value on the date of the grant. The options have vesting periods ranging from one to four years and expire between five and ten years from the date of the grant. At December 31, 2005, the Company had issued 584 unexercised options to employees and directors to purchase common shares under its stock-based compensation plans.

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

A summary of the status of the Company's stock option plans as of December 31, 2005, 2004 and 2003, and changes during the years ending on those dates is presented below:

	2005		2004		2003	
	Number of Options	Weighted- Average Exercise Price	Number of Options	Weighted- Average Exercise Price	Number of Options	Weighted- Average Exercise Price
<b>Options</b>						
Outstanding at beginning of year	574	U.S. \$4.51	855	U.S. \$4.42	974	U.S. \$4.59
Granted	118	20.28	5	11.81	186	2.29
Exercised	(105)	5.73	(276)	4.41	(301)	3.69
Forfeited	(3)	8.67	(10)	2.28	(4)	3.85
Outstanding at end of year	<u>584</u>	<u>U.S. \$7.46</u>	<u>574</u>	<u>U.S. \$4.51</u>	<u>855</u>	<u>U.S. \$4.42</u>
Options exercisable at end of year	<u>330</u>	<u>U.S. \$4.94</u>	<u>313</u>	<u>U.S. \$6.24</u>	<u>449</u>	<u>U.S. \$6.35</u>

The following table summarizes information about the stock option plans as of December 31, 2005:

	Options Outstanding			Options Exercisable	
	Number Outstanding	Weighted- Average Remaining Contractual Life	Weighted- Average Exercise Price	Number Exercisable	Weighted- Average Exercise Price
<b>Range of Exercise Prices</b>					
U.S. \$32.50	6	4.6 years	U.S. \$32.50	—	U.S. \$32.50
\$13.16 to \$19.61	113	4.4	19.50	—	13.16
\$7.50 to \$11.25	160	1.6	7.87	158	7.85
\$4.00 to \$4.94	3	7.3	4.63	1	4.62
\$2.25 to \$3.44	260	6.5	2.37	129	2.44
\$1.38 to \$2.00	<u>42</u>	4.7	1.63	<u>42</u>	1.63
U.S. \$1.38 to \$32.50	<u>584</u>	4.6	U.S. \$7.46	<u>330</u>	U.S. \$4.94

The Company granted approximately 144 stock options to purchase common shares to employees on April 28, 2006. The options have an exercise price of U.S. \$ 39.58, vest over four years and expire five years from the date of grant.

The following table represents the potential dilutive effect of options which have been issued, and could be exercised by the option holder.

	Year Ended December 31,		
Number of Common Shares	2005	2004	2003
Weighted average common shares outstanding (basic)	8,298	8,063	7,723
Dilutive effect of options	<u>465</u>	<u>437</u>	<u>260</u>
Weighted average common shares outstanding (diluted)	<u>8,763</u>	<u>8,500</u>	<u>7,983</u>

In the years ended December 31, 2005, 2004 and 2003, there were 6, nil, and 338 options, respectively, excluded from the calculation, due to an anti-dilutive effect as a result of the exercise price being higher than the market price of the stock in the period.

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

### NOTE 12 MAJOR CUSTOMERS, EXPORT SALES AND SUPPLIERS

Certain major customers accounted for significant portions of the sales from continuing operations. The table below reflects customers whose purchases represented more than 10% of the Company's total revenues in any of the periods indicated.

Sales by Major Customer	Year Ended December 31,		
	2005	2004	2003
Customer A .....	\$11,211	\$ 8,631	\$ 2,328
Customer B .....	6,736	4,157	1,744
Customer C .....	6,554	5,684	4,631
Customer D .....	4,102	8,150	1,946
Customer E .....	2,893	3,333	4,219
	<u>\$31,496</u>	<u>\$29,955</u>	<u>\$14,868</u>
Percentage of total revenue .....	<u>50%</u>	<u>56%</u>	<u>38%</u>

Accounts receivable and related party receivables related to these major customers at December 31 were \$4,683 in 2005 and \$5,855 in 2004.

Sales by Geographic Market	Year Ended December 31					
	2005		2004		2003	
U.S.A. ....	\$25,671	41%	\$25,105	46%	\$19,437	50%
Europe .....	17,924	28%	13,852	26%	7,793	20%
Asia/Australia .....	13,530	21%	10,331	19%	8,367	22%
Canada .....	4,462	7%	3,044	6%	2,753	7%
Other .....	1,708	3%	1,600	3%	334	1%
	<u>\$63,295</u>	<u>100%</u>	<u>\$53,932</u>	<u>100%</u>	<u>\$38,684</u>	<u>100%</u>

Certain of the Company's products incorporate components that are either procured from sole source suppliers or which are in short supply. In the opinion of management, the Company has taken measures to mitigate the risk associated with the availability of these components.

### NOTE 13 SHARE OFFERING COSTS

In the year ended December 31, 2004, the Company incurred \$754 of expenses in relation to a proposed public offering in Canada and a private placement in the U.S. of its common shares. On May 26, 2004, the Company withdrew the offering and expensed the costs.

### NOTE 14 OTHER EXPENSE

	Year Ended December 31,		
	2005	2004	2003
Financing charge on sales by Point .....	\$(71)	\$(70)	\$ (83)
Miscellaneous .....	<u>(1)</u>	<u>3</u>	<u>(54)</u>
	<u>\$(72)</u>	<u>\$(67)</u>	<u>\$(137)</u>

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

### NOTE 15 INCOME TAXES

The Company follows the liability method of accounting for income taxes. Temporary differences that give rise to future income tax assets and liabilities as of December 31 are as follows:

	<u>2005</u>	<u>2004</u>
Future income tax assets		
Loss carryforwards .....	\$ 1,730	\$ 1,650
Scientific research deductions and credits .....	46,110	49,725
Reserves not currently deductible for tax .....	1,710	1,500
Capital assets .....	970	1,500
Capital losses .....	150	150
Deferred gain on sale of building .....	<u>120</u>	<u>150</u>
	50,790	54,675
Future income tax liabilities		
Intangible assets .....	(400)	(275)
Deferred development costs .....	(560)	(800)
Deferred gain on hedging contracts .....	<u>(50)</u>	<u>(50)</u>
	(1,010)	(1,125)
Valuation allowance .....	<u>(44,189)</u>	<u>(50,361)</u>
	<u>\$ 5,591</u>	<u>\$ 3,189</u>
Future income tax asset — current portion .....	2,370	1,286
Future income tax asset — long term portion .....	<u>3,221</u>	<u>1,903</u>
	<u>\$ 5,591</u>	<u>\$ 3,189</u>

As at December 31, 2005, the Company's net future income tax assets were \$5,591, reflecting temporary differences between the financial reporting and tax treatment of certain current assets and liabilities and non-current assets and liabilities, in addition to the tax benefit of net operating and capital loss carryforwards and tax credit carryforwards.

In accordance with the CICA Handbook Section 3465, "Accounting for Income Taxes", the Company reviews all available positive and negative evidence to evaluate the recoverability of the future income tax assets. This includes a review of such evidence as the carryforward periods of the significant tax assets, the Company's history of generating taxable income in its material tax jurisdictions and the Company's forecasted profitability in the foreseeable future. Based on this review the Company concluded that the valuation allowance as at December 31, 2005 was appropriate and determined that it was more likely than not that the recorded future income tax assets would be realized.

On April 11, 2006, the government of Alberta proposed changes to the provincial tax laws, including a reduction in the provincial corporate tax rate from 11.5% to 10%, effective April 1, 2006.

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

The following table reconciles the differences between the income tax that would result solely by applying statutory rates and the income tax provided for in the statements of operations.

	Year Ended December 31,					
	2005		2004		2003	
Income from continuing operations						
before income taxes .....	\$16,360		\$14,031		\$ 3,152	
Statutory income tax expense .....	\$ 5,500	33.6%	\$ 4,752	33.9%	\$ 1,169	37.1%
Adjusted for the effects of:						
Change in valuation allowance on						
tax benefit .....	(6,172)		(5,339)		(2,377)	
Change in tax rates on future						
tax benefit .....	—		1,604		1,005	
Non deductible capital loss .....	—		—		162	
Non deductible expenses and costs ..	258		166		34	
Other .....	46		(17)		—	
Large corporation tax .....	12		71		59	
Total income tax expense (benefit) .....	\$ (356)	2.2%	\$ 1,237	8.8%	\$ 52	1.6%

### a) Canadian Income Taxes

At December 31, 2005, the Company has approximately \$139 million of research and development costs deducted in the accounts, in excess of amounts claimed for Canadian federal income tax purposes and approximately \$124 million of research and development costs deducted in the accounts, in excess of amounts claimed for provincial income tax purposes.

At December 31, 2005, the Company also has unutilized investment tax credits of approximately \$2.9 million available to reduce future Canadian federal income taxes. These credits expire as follows:

2013 .....	\$ 500
2014 .....	900
2015 .....	700
2016 .....	800
	<u>\$2,900</u>

The Company has determined that CMC Electronics' acquisition of a majority of the common shares of the Company on April 17, 1998, BAE SYSTEMS p.l.c.'s acquisition of the majority of the common shares of CMC Electronics on November 29, 1999 and ONCAP's acquisition of the common shares of CMC Electronics on April 11, 2001, constitute acquisitions-of-control of the Company for Canadian income tax purposes. Accordingly, the availability of certain of the Company's Canadian losses, deductions, and investment tax credits may be subject to limitation.

The ultimate availability and amount of the losses and other tax benefits described above may be dependent upon future Canada Revenue Agency audits. An adverse determination could result in a significant decrease in the availability and amount of the tax benefits described above.

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

### NOTE 16 RELATED PARTY TRANSACTIONS

In the normal course of business, the Company had the following transactions, measured at the exchange amount, with its related parties:

	Year Ended December 31,		
	2005	2004	2003
Product sales to Point, Inc. ....	\$2,247	\$2,178	\$1,590
Services provided to Point, Inc. ....	153	137	133
Engineering and other services charged by Point, Inc. ....	611	265	87
Engineering services charged to Point, Inc. ....	913	309	—
Inventory purchases from CMC Electronics, Inc. and Point, Inc. ....	12	1,272	2,809
Inventory sold to CMC Electronics, Inc. ....	124	85	—
Contracted development costs charged by CMC Electronics, Inc. ....	—	218	523
Product sales and engineering services charged to CMC Electronics, Inc. ....	—	—	54
Other charges from CMC Electronics, Inc. ....	10	318	408
Royalties charged to CMC Electronics, Inc. ....	241	545	261
Royalties paid to CMC Electronics, Inc. ....	—	261	82
Share offering costs charged to CMC Electronics, Inc. ....	—	748	—
Share offering costs charged by CMC Electronics, Inc. ....	—	55	—
Consulting fees charged by Dave Vaughn, after resignation as CEO in February 2002 ....	—	—	38

Significant related party receivables at December 31, 2005 consist of \$1,331 from Point, Inc. (\$1,318 at December 31, 2004). Related party payables at December 31, 2005 consist of amounts due to Point, Inc. of \$15 (\$55 at December 31, 2004).

The related party notes receivable of \$1,552 at December 31, 2005 (\$1,614 at December 31, 2004) reflects the Company's proportionate joint venture interest in the aggregate borrowings by Point, Inc. from NovAtel and Sokkia Co., Ltd. (Sokkia) of U.S. \$5,330. The loans are secured by the assets of Point, Inc. and bore interest at 3% during 2005 (3% in 2004 and 2003). On February 3, 2006, the Company and Sokkia agreed to extend the due dates on the loans to August 31, 2006 (see Note 17).

During 2003, the Company and Sokkia advanced U.S. \$500 in new loans to Point, Inc. with the Company's share being U.S. \$245.

On May 14, 2003, the Company acquired CMC Electronics' non-aviation Global Positioning System (GPS) OEM product line. The purchase price was comprised of \$150 at closing and \$600 payable over time as a royalty on the revenue generated by this product line. The fair value of net assets acquired was as follows:

Capital assets .....	\$150
Intangibles .....	497
Total investment .....	<u>\$647</u>

From January 2005 through August 2005, CMC Electronics sold its interest in NovAtel and does not maintain any representation on the Company's board of directors and therefore is not considered to be a related party, effective May 11, 2005.



## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

### NOTE 17 INVESTMENT IN POINT, INC.

On July 20, 1999, the Company and Sokkia Co., Ltd. formed a joint venture, Point, Inc., to distribute GPS based products for surveying, mapping, geographical information systems, construction and construction machine control applications, on a worldwide basis. The consolidated financial statements presented herein include the Company's proportionate share of the accounts of Point, Inc.

The following is a summary of the Company's 49% proportionate share of the financial position, operating results, and cash flows of Point, Inc.:

	Year ended December 31,		
	2005	2004	2003
<b>Financial Position</b>			
Current assets .....	\$1,332	\$1,603	\$1,728
Non-current assets .....	118	104	100
Total assets .....	<u>\$1,450</u>	<u>\$1,707</u>	<u>\$1,828</u>
Current liabilities .....	<u>\$2,729</u>	<u>\$2,635</u>	<u>\$2,818</u>
Total liabilities .....	<u>\$2,729</u>	<u>\$2,635</u>	<u>\$2,818</u>
<b>Results of Operations</b>			
Revenues .....	\$5,819	\$5,932	\$6,097
Gross profit .....	1,726	1,760	1,501
Expenses .....	2,094	1,781	1,535
Income (loss) .....	(368)	(21)	(34)
<b>Cash Flows</b>			
Cash provided by (used in)			
Operating activities .....	\$ 100	\$ 62	\$ 32
Investing activities .....	(68)	(23)	(7)
Financing activities .....	(11)	9	142
Effect of exchange rate changes on financing activities .....	(51)	(118)	(351)

Included in current liabilities is the Company's share of notes payable by Point, Inc. to Sokkia, in the amount of \$1,552 (\$1,614 at December 31, 2004). The loans are secured by the assets of Point, Inc., and bore interest at 3% during 2005 (3% in 2004 and 2003). On February 3, 2006, the Company and Sokkia agreed to extend the due dates on the loans to August 31, 2006.

Point, Inc. is dependent on the Company and Sokkia for product supply, distribution and financing. Should Sokkia and the Company discontinue their support, Point, Inc.'s ability to continue as a going concern would be impaired. If the existing loans to Point, Inc. of U.S. \$ 5,330 were ultimately not repaid by Point, Inc. to the Company and Sokkia, and/or if Point, Inc. were liquidated in an orderly wind-down, the Company believes that its maximum loss exposure in the statement of operations related to Point, Inc., as of December 31, 2005, after consideration of the effects of the proportionate consolidation of Point, Inc., would be approximately \$600, comprised primarily of working capital related items and the costs that would be incurred to cease operations. These financial statements do not reflect any adjustment that would be required if Point, Inc.'s operations were not considered a going concern.

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

### NOTE 18 DISCONTINUED OPERATIONS (MEZURE, INC.)

As of December 31, 2005, the Company owned a 70% equity interest in Mezure, Inc. ("Mezure"), a company that had been developing a GPS, wireless communication and Internet-based product for deformation monitoring of manmade and natural structures.

During the latter part of 2002, the Company discontinued its financial support of Mezure. On April 8, 2003, the shareholders of Mezure voted unanimously to proceed with a Chapter 7 bankruptcy, which was filed on June 25, 2003. On September 24, 2003 an Order Approving Trustee's Account, Discharging Trustee and Closing Estate was entered into the docket of the United States Bankruptcy Court, District Oregon (Portland). Consequently, the Company treated Mezure as a discontinued operation.

With the Chapter 7 bankruptcy filing concluding, the Company recognized a gain of \$379 relating to the liquidation of the residual assets and liabilities of Mezure in the year ended December 31, 2003. While Mezure operated as a separate corporation, Mezure's third party creditors could potentially attempt to satisfy their claims with Mezure by pursuing these claims against the Company. The Company believes that these claims would not be valid and that the ultimate liability with respect to the resolution of these actions is not expected to materially affect the Company's financial position or results of operations.

The income (loss) from discontinued operations pertaining to Mezure for the years ended on December 31 is as set forth below:

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Revenues .....	\$—	\$—	\$ 34
Cost of sales.....	—	—	(1)
Research and development expenses.....	—	—	(27)
Selling and marketing expenses.....	—	—	(32)
General and administration expenses .....	—	21	(112)
Other income .....	—	—	119
Gain on liquidation of assets and liabilities .....	—	—	379
Income from discontinued operations .....	<u>—</u>	<u>\$21</u>	<u>\$ 360</u>

The consolidated balance sheets as of December 31, 2005 and December 31, 2004 include residual accounts payable and accrued liabilities related to discontinued operations of \$15.

### NOTE 19 ACQUISITION OF CMC ELECTRONICS' OEM GPS PRODUCT LINE

On May 14, 2003, the Company acquired CMC Electronics Inc.'s non-aviation Global Positioning System (GPS) OEM product line. The purchase price was comprised of \$150 at closing and \$600 payable over time (of which \$564 has been paid to December 31, 2005) as a royalty on the revenue generated by this business. The fair value of net assets acquired is as follows:

Capital assets .....	\$150
Intangibles.....	<u>497</u>
Total investment.....	<u>\$647</u>

The intangibles are comprised primarily of technology and an established market presence to which the Company has assigned values of \$149 and \$348, respectively. The Company estimates that these intangibles will have an expected useful life of 4 years and will be amortized using the straight-line method.

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

At the time of the acquisition, CMC Electronics owned approximately 58% of the Company's outstanding common shares and accordingly was a related party. The acquisition of the CMC Electronics' GPS OEM product line was reviewed and approved by a committee of independent directors established by the Company's Board of Directors.

### NOTE 20 ACQUISITION OF WAYPOINT CONSULTING INC.

On October 1, 2005 the Company acquired all of the shares of Waypoint Consulting Inc. ("Waypoint") for approximately \$3.5 million in cash, subject to post-closing adjustments to working capital. Of the total purchase price, \$2.2 million was paid by December 31, 2005 and \$1.2 million was held in escrow by Waypoint's attorneys and will be paid in installments over three years, subject to certain conditions. Waypoint's products include specialized real-time and post-processing GPS and GPS/inertial positioning and trajectory software. The results of the Waypoint acquisition have been included in the consolidated results of operations since October 1, 2005.

The fair value of net assets and liabilities acquired has been allocated on a preliminary basis as follows:

Accounts receivable .....	\$ 384
Inventories .....	22
Prepaid expenses .....	22
Capital and intangible assets .....	46
Intangibles related to technology, brand names and customer relationships .....	1,818
Goodwill .....	1,494
Accounts payable .....	(82)
Deferred revenue .....	<u>(173)</u>
Net investment .....	<u>\$3,531</u>

The intangibles are comprised primarily of technology, customer relationships and brand names to which the Company has assigned values of \$1,260 and \$358 and \$200 respectively. The Company estimates that these intangibles have an average expected useful life of 8.5 years and will be amortized using the straight-line method. The Company does not expect the \$1,494 of goodwill to be deductible for tax purposes.

The following unaudited pro forma information gives effect to the acquisition of Waypoint as if it had occurred on January 1, 2004.

	Year Ended December 31, 2005		
	As presented	Waypoint Acquisition	Pro forma
Revenues .....	\$63,295	\$1,360	\$64,655
Net income .....	\$16,716	\$ 203	\$16,919
Net income per share (basic) .....	\$ 2.01	\$ 0.03	\$ 2.04
Net income per share (diluted) .....	\$ 1.91	\$ 0.02	\$ 1.93

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

	Year Ended December 31, 2004		
	As presented	Waypoint Acquisition	Pro forma
Revenues .....	\$53,932	\$1,785	\$55,717
Net income .....	\$12,815	\$ 376	\$13,191
Net income per share (basic) .....	\$ 1.59	\$ 0.05	\$ 1.64
Net income per share (diluted) .....	\$ 1.51	\$ 0.04	\$ 1.55

### NOTE 21 CONSOLIDATED STATEMENTS OF CASH FLOWS

The net changes in non-cash working capital related to operations include:

	Year Ended December 31,		
	2005	2004	2003
(Increase) decrease in accounts receivable and related party receivables .....	\$ (694)	\$(3,480)	\$2,876
(Increase) in inventories .....	(223)	(409)	(71)
(Increase) decrease in prepaid expenses and deposits .....	(309)	89	(84)
Increase in accounts payable, accrued liabilities and related party payables .....	222	2,699	677
(Decrease) increase in deferred revenue .....	(176)	443	(192)
Increase in provision for future warranty costs .....	155	128	66
Net change in non-cash working capital .....	<u>\$(1,025)</u>	<u>\$ (530)</u>	<u>\$3,272</u>

### NOTE 22 STOCK-BASED COMPENSATION

At December 31, 2005, the Company had issued 584 unexercised options to employees and directors to purchase common shares under its stock-based compensation plans (see Note 11).

Effective January 1, 2004, the Company adopted the fair value method of accounting for stock options awarded to employees on or after January 1, 2002, as required by amended CICA Handbook Section 3870 *Stock-Based Compensation and Other Stock-Based Payments*. As permitted by the transitional provisions of Section 3870, the change was adopted retroactively without restatement. Under Section 3870, the fair value of stock options is recognized over the applicable vesting period as a charge to stock-based compensation expense and a credit to contributed surplus. For the year ended December 31, 2005 stock-based compensation expense of \$587 (\$326 in the year ended December 31, 2004) was recognized. When options are exercised, the proceeds are credited to share capital, and the applicable fair value is reclassified from contributed surplus to share capital. As of December 31, 2005, \$363 was reclassified from contributed surplus to share capital, as a result of stock option exercises.

Prior to the Company's adoption of the amended provisions of Section 3870 on January 1, 2004, the Company applied an intrinsic value based method to account for its stock-based compensation plans, and no compensation cost was recognized within the statement of operations for the year ended December 31, 2003. Had compensation cost for the Company's stock-based compensation plans been determined based on the fair value of the options at the grant dates, the Company's pro-forma net income and net income per share would have been as follows for the year ended December 31, 2003:

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

	Year Ended December 31, 2003	
Net income from continuing operations .....	As reported	\$3,100
	Pro forma	\$2,637
Basic net income from continuing operations per share .....	As reported	\$ 0.40
	Pro forma	\$ 0.34
Diluted net income from continuing operations per share .....	As reported	\$ 0.39
	Pro forma	\$ 0.33
Net income .....	As reported	\$3,460
	Pro forma	\$2,997
Basic net income per share .....	As reported	\$ 0.45
	Pro forma	\$ 0.39
Diluted net income per share .....	As reported	\$ 0.43
	Pro forma	\$ 0.38

The fair value of each option granted is estimated using the Black-Scholes option pricing model with the following weighted-average assumptions used for options granted in 2005, 2004 and 2003: dividend yield of 0%; expected lives of 3 to 10 years; a risk free interest rate of between 3.34% and 4.3% and expected volatility of between 84% to 98%.

The weighted average fair value of options granted was U.S. \$9.61 in 2005, (U.S. \$10.67 in 2004 and U.S. \$2.06 in 2003.)

### *Phantom Share Plan*

Effective January 1, 2004, the Company established a new Long Term Incentive Plan (LTI Plan), which authorized the grant of approximately 44 thousand phantom shares to employees of the Company. All grants of phantom shares under the LTI Plan have a three-year cliff vesting and would vest on December 31, 2006, if certain performance objectives are achieved. Payments under the LTI plan are made in cash.

As of December 31, 2005, the Company estimated that the fair value of the granted and outstanding phantom shares was \$1,441, based on a 20-day average price of the Company's common shares.

For the year ended December 31, 2005, the Company recognized \$347 in compensation expense related to phantom shares (\$615 in the year ended December 31, 2004).

## **NOTE 23 DIFFERENCES BETWEEN CANADIAN AND UNITED STATES GENERALLY ACCEPTED ACCOUNTING PRINCIPLES**

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles in Canada (Canadian GAAP or Canadian principles). The significant differences from U.S. generally accepted accounting principles (U.S. GAAP or U.S. principles) are as follows:

### a) *Deferred Development Costs* (see Note 7)

In the year ended December 31, 2005, the Company deferred \$nil of development costs (\$218 in 2004 and \$157 in 2003) in accordance with Canadian GAAP. Under U.S. GAAP, these costs would be expensed as incurred as research and development costs.

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

In the year ended December 31, 2005, the Company amortized \$538 of deferred development costs (\$416 in 2004 and \$196 in 2003) in accordance with Canadian GAAP. Under U.S. GAAP, these costs would have been expensed in the periods when the originating expenditures were incurred.

Further, for U.S. GAAP purposes, the Company would have recharacterized the goodwill acquired on the Mezure, Inc. share acquisition of \$231 as development related costs, and these costs would have been expensed on acquisition in 2001.

In addition, for Canadian GAAP purposes, in connection with the recognition of prior year's investment tax credits, the Company reduced the deferred development costs by \$164 in the year ended December 31, 2005. Under U.S. GAAP, this amount would have been accounted for as an expense when the originating expenditures were incurred.

### b) *Stock-Based Compensation*

Under U.S. GAAP, Statement of Financial Accounting Standards ("SFAS") 123 "Accounting for Stock-Based Compensation" establishes a fair value based method of accounting for stock-based compensation. Companies have the option of including the effect of this pronouncement in determining their net income, or alternatively, may continue to apply the accounting provisions of APB Opinion 25, but must comply with the disclosure requirements of SFAS 123. For U.S. GAAP purposes, the Company continues to account for its stock-based compensation in accordance with APB Opinion 25 (see Note 23 (k)).

Effective January 1, 2004, under Canadian GAAP the Company adopted the fair value method of accounting for stock options awarded to employees on or after January 1, 2002 as required by amended CICA Handbook Section 3870 *Stock-Based Compensation and Other Stock-Based Payments*. As permitted by the transitional provisions of Section 3870, the change was adopted retroactively without restatement. Under Section 3870, the fair value of stock options is recognized over the applicable vesting period as stock-based compensation expense and a credit to contributed surplus. When options are exercised, the proceeds are credited to share capital, and the applicable fair value is reclassified from contributed surplus to share capital. Retroactive application of Section 3870 resulted in the opening balances as at January 1, 2004 of deficit, contributed surplus and share capital being increased by \$456, \$390 and \$66, respectively, as though the fair value method had been applied since January 1, 2002. As indicated above, the Company continues to account for its stock-based compensation in accordance with APB 25 and thus these adjustments would not be recorded for U.S. GAAP purposes.

Under Canadian GAAP, the Company incurred stock-based compensation expense of \$587 in the year ended December 31, 2005 (\$326 in 2004). For U.S. GAAP purposes, this expense would not have been included in the determination of net income.

### c) *Derivatives and Hedging Activities*

The Company has historically entered into forward foreign exchange contracts to manage its exposure to foreign currency fluctuations. Under U.S. GAAP the accounting for derivative instruments and hedging activities is contained in the Statement of Financial Accounting Standard ("SFAS") No. 133, as amended by SFAS 137, SFAS 138 and SFAS 149 ("SFAS 133"). SFAS 133 establishes accounting and reporting standards requiring that all derivative instruments be recorded in the balance sheet as either an asset or a liability measured at fair value and requires that changes in the fair value be recognized currently in earnings unless specific hedge accounting criteria are met. For cash flow hedges, changes in the fair value of the derivative instrument are recognized in net earnings in the same period as the hedged item and

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

any changes in the fair value prior to that period are recognized in other comprehensive income. For fair value hedges, both the derivative instrument and the underlying commitment are recognized on the balance sheet at their fair value and any changes in the fair value are recognized currently in net earnings. The Company's foreign exchange contracts have been accounted for as cash flow hedges.

Under U.S. GAAP, SFAS 133 would result in an increase in total assets of \$192 as of December 31, 2005 (\$179 as of December 31, 2004) related to the fair value of the Company's foreign exchange contracts.

### d) *Investment in Joint Ventures*

The accounts of the Company's 49.0% joint venture interest in Point, Inc. are proportionately consolidated as required under Canadian GAAP. Under U.S. GAAP, proportionate consolidation is not permitted, and the Company's investment in these joint ventures would be accounted for using the equity method. As permitted by SEC guidance, the effects of this difference in accounting principles have not been reflected in the accompanying tables (see Note 17).

In 2003, the Company recognized a gain of \$379 related to the liquidation of the remaining assets and liabilities of Mezure (see Note 18). Under U.S. GAAP, this gain would have been \$571, since \$192 characterized as goodwill under Canadian GAAP would have expensed on acquisition in 2001 (see Note 23(a)).

### e) *Intangibles Related to Acquisition of CMC Electronics OEM GPS Business*

On May 14, 2003, the Company acquired the CMC Electronics non-aviation GPS product line (see Note 19). The fair value of the net assets acquired included \$497 in intangibles, comprised primarily of technology, product design, customer relationships and an established market presence. Under U.S. GAAP, when accounting for a transfer of assets between entities under common control, the entity that receives the net assets or the equity interest would initially recognize the assets and liabilities transferred at their carrying amounts at the date of transfer. Any excess of consideration given over the controlling shareholders' carrying value would be accounted for as a reduction of equity.

### f) *Provision for Future Warranty Costs*

The changes in the provision for future warranty costs during each of the years ended December 31, 2005, 2004 and 2003 are as follows:

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Opening balance, beginning of period .....	\$ 538	\$ 410	\$ 344
Additions to provision .....	382	312	220
Costs incurred .....	<u>(227)</u>	<u>(184)</u>	<u>(154)</u>
Ending balance, end of period .....	<u>\$ 693</u>	<u>\$ 538</u>	<u>\$ 410</u>

### g) *Investment Tax Credits*

Under Canadian GAAP, the Company uses the cost reduction method to account for its investment tax credits. The investment tax credits relate to certain research and development expenses and are recognized when there is reasonable assurance that the Company will be able to realize the benefit of these credits. In the year ended December 31, 2005, the Company recognized \$1,756 (\$4,356 in 2004, \$nil in 2003) of investment tax credits, of which \$1,592 was recorded on the statement of operations as a benefit of investment tax credits on the statement of operations and \$164 was recorded as a reduction of deferred development costs on the balance sheet.

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

Under U.S. GAAP, the Company would use the flow through method to account for its investment tax credits and would record the recognition of the \$1,756 of investment tax credits in 2005 as a reduction of the current income tax provision. Under U.S. GAAP, for the year ended December 31, 2004, the Company would record the recognition of the \$4,356 of investment tax credits as a \$2,258 reduction of the current income tax provision and as a \$2,098 increase in future income tax benefit.

The net effect of these reconciling items would be an increase in net income from continuing operations of \$164 in the year ended December 31, 2005 under U.S. GAAP.

### h) *Comprehensive Income*

U.S. GAAP utilizes the concept of comprehensive income, which includes net income and other comprehensive income. Currently, there is no similar concept in effect under Canadian GAAP. Other comprehensive income represents the change in equity during the period from transactions and other events from non-owner sources and includes such items as changes in the fair value of cash flow hedges.

### i) *Summary of the Differences Between Canadian and U.S. GAAP*

The effects of the above-noted differences between Canadian and U.S. GAAP on the statements of operations and on the balance sheets are as follows:

	Year Ended December 31,		
	2005	2004	2003
<b>Net income from continuing operations —</b>			
<b>Canadian GAAP</b> .....	\$16,716	\$12,794	\$3,100
Adjustments to U.S. GAAP			
Deferred development costs (a) .....	—	(218)	(157)
Amortization of deferred development costs (a) .....	538	416	196
Reduction of deferred development costs related to			
recognition of investment tax credits (a)(g) .....	164	—	—
Stock-based compensation expense (b) .....	587	326	—
Amortization of intangibles acquired from			
CMC Electronics (e) .....	124	124	62
<b>Net income from continuing operations — U.S. GAAP ..</b>	<b>18,129</b>	<b>13,442</b>	<b>3,201</b>
<b>Net income from discontinued operations —</b>			
<b>Canadian GAAP</b> .....	—	21	360
Adjustment to U.S. GAAP			
Gain on liquidation of Mezure, Inc. (d) .....	—	—	192
<b>Income from discontinued operations — U.S. GAAP .....</b>	<b>—</b>	<b>21</b>	<b>552</b>
<b>Net income — U.S. GAAP</b> .....	<b><u>18,129</u></b>	<b><u>13,463</u></b>	<b><u>3,753</u></b>
Net unrealised gain (loss) on foreign			
exchange contracts (c) .....	192	179	—
Reclassification to income of gains and losses			
on cash flow hedges (c) .....	(179)	—	48
<b>Comprehensive income</b> .....	<b><u>\$18,142</u></b>	<b><u>\$13,642</u></b>	<b><u>\$3,801</u></b>



# Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

	December 31,	
	2005	2004
<b>Total Assets</b>		
Canadian GAAP .....	\$71,255	\$52,946
Adjustments to U.S. GAAP		
Deferred development costs (a) .....	(1,657)	(2,359)
Fair value of financial instruments (c) .....	192	179
Reduction of intangibles acquired from CMC Electronics to carrying value (e) .....	(182)	(306)
U.S. GAAP .....	<u>\$69,608</u>	<u>\$50,460</u>
<b>Total Shareholders' Equity</b>		
Canadian GAAP .....	\$58,117	\$40,093
Adjustments to U.S. GAAP		
Deferred development costs (a) .....	(1,657)	(2,359)
Reduction of intangibles acquired from CMC Electronics to carrying value (e) .....	(492)	(492)
Amortization of intangibles acquired from CMC Electronics (e) ...	310	186
U.S. GAAP — before other comprehensive income .....	<u>56,278</u>	<u>37,428</u>
Accumulated other comprehensive income .....	192	179
U.S. GAAP — including accumulated other comprehensive income ....	<u>\$56,470</u>	<u>\$37,607</u>

## j) *Net Income (Loss) per Share*

Net income (loss) per share as computed under Canadian and U.S. principles is as set forth below for the following periods:

	Year Ended December 31,					
	Canadian GAAP			U.S. GAAP		
	Net Income per Share — Basic			Net Income per Share — Basic		
	2005	2004	2003	2005	2004	2003
Continuing operations .....	\$2.01	\$1.59	\$0.40	\$2.18	\$1.67	\$0.41
Discontinued operations ...	—	—	0.05	—	—	0.08
Net income per share .....	<u>\$2.01</u>	<u>\$1.59</u>	<u>\$0.45</u>	<u>\$2.18</u>	<u>\$1.67</u>	<u>\$0.49</u>
	Net Income per Share — Diluted			Net Income per Share — Diluted		
	2005	2004	2003	2005	2004	2003
Continuing operations .....	\$1.91	\$1.51	\$0.39	\$2.07	\$1.58	\$0.40
Discontinued operations ...	—	—	0.04	—	—	0.07
Net income per share .....	<u>\$1.91</u>	<u>\$1.51</u>	<u>\$0.43</u>	<u>\$2.07</u>	<u>\$1.58</u>	<u>\$0.47</u>

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

### k) *Stock-Based Compensation*

Statement of Financial Accounting Standards (SFAS) 123 "Accounting for Stock-Based Compensation" establishes a fair value based method of accounting for stock-based compensation. Companies have the option of including the effect of this pronouncement in determining their net income, or alternatively, may continue to apply the accounting provisions of APB Opinion 25, but must comply with the disclosure requirements of SFAS 123 and SFAS 148. Had the Company prepared its consolidated financial statements in accordance with U.S. GAAP, the Company would have accounted for its stock-based compensation in accordance with APB Opinion 25.

At December 31, 2005, the Company had 584 options outstanding that had been issued to employees and directors (574 in 2004 and 855 in 2003) to purchase common shares under its stock-based compensation plans (see Note 11). As the Company would have applied APB Opinion 25 and related interpretations in accounting for its plans, no compensation expense would have been recognized within the statement of operations under U.S. GAAP in 2005, 2004 and 2003. Had compensation expense for the Company's stock-based compensation plans been determined based on the fair value of the options at the grant dates, the Company's pro forma net income from continuing operations and net income per share would have been as follows:

		Year Ended December 31		
		2005	2004	2003
Net income from continuing operations —				
U.S. GAAP .....	As reported	\$18,129	\$13,442	\$3,201
Less: Fair value of stock options .....		<u>502</u>	<u>408</u>	<u>463</u>
Net income from continuing operations —				
U.S. GAAP .....	Pro forma	<u>\$17,627</u>	<u>\$13,034</u>	<u>\$2,738</u>
Net income from continuing operations —	As reported	\$ 2.18	\$ 1.67	\$ 0.41
earnings per share (basic) .....	Pro forma	\$ 2.12	\$ 1.62	\$ 0.35
Net income from continuing operations —	As reported	\$ 2.07	\$ 1.58	\$ 0.40
earnings per share (diluted) .....	Pro forma	\$ 2.01	\$ 1.53	\$ 0.34
Net income — U.S. GAAP .....	As reported	\$18,129	\$13,463	\$3,753
Less: Fair value of stock options .....		<u>502</u>	<u>408</u>	<u>463</u>
Net income — U.S. GAAP .....	Pro forma	<u>\$17,627</u>	<u>\$13,055</u>	<u>\$3,290</u>
Net income — earnings per share (basic) ....	As reported	\$ 2.18	\$ 1.67	\$ 0.49
	Pro forma	\$ 2.12	\$ 1.62	\$ 0.43
Net income — earnings per share (diluted) ..	As reported	\$ 2.07	\$ 1.58	\$ 0.47
	Pro forma	\$ 2.01	\$ 1.54	\$ 0.41

The fair value of each option granted is estimated using the Black-Scholes option pricing model with the following weighted-average assumptions used for options granted in 2005, 2004 and 2003: dividend yield of 0%; expected lives of 3 to 10 years; a risk free interest rate of between 3.34% and 4.3%, and expected volatility of between 84% to 98%.

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

### l) Consolidated Statement of Cash Flows

The effects of the differences between Canadian and U.S. GAAP on the consolidated statement of cash flows are as follows:

	Year Ended December 31		
	2005	2004	2003
Cash flow provided by operations — Canadian GAAP .....	\$ 17,092	\$12,504	\$ 8,013
Adjustments to U.S. GAAP			
Deferred development costs (a) .....	—	(218)	(157)
Royalty payment relating to CMC Electronics' OEM			
GPS business (e) .....	(221)	(261)	(82)
Cash flow provided by operations — U.S. GAAP .....	\$ 16,871	\$12,025	\$ 7,774
Cash flow provided by financing activities — Canadian GAAP	\$ 778	\$ 598	\$ 1,308
Adjustments to U.S. GAAP .....	—	—	—
Cash flow provided by financing activities — U.S. GAAP ..	\$ 778	\$ 598	\$ 1,308
Cash used in investing activities — Canadian GAAP .....	\$(24,098)	\$(6,598)	\$(8,576)
Adjustments to U.S. GAAP			
Deferred development costs (a) .....	—	218	157
Royalty payment relating to CMC Electronics' OEM			
GPS business (e) .....	221	261	82
Cash used in investing activities — U.S. GAAP .....	\$(23,877)	\$(6,119)	\$(8,337)

### m) Accounts Payable and Accrued Liabilities

The following balances comprise accounts payable and accrued liabilities:

	Year Ended December 31,	
	2005	2004
Accounts payable and accrued trade liabilities .....	\$5,229	\$4,327
Accrued salaries, incentive plans and other employee-related obligations ..	3,686	4,031
Accrued dealer and agent commissions .....	458	271
Other .....	411	519
Total .....	\$9,784	\$9,148

### n) New Canadian and U.S. GAAP Accounting Pronouncements

#### Canadian Pronouncements

In January 2005, the Canadian Institute of Chartered Accountants ("CICA") issued Section 1530, "Comprehensive Income", Section 3251, "Equity", Section 3855, "Financial Instruments — Recognition and Measurement" and Section 3865, "Hedges". The new standards increase harmonization with US GAAP and will require the following:

- Financial assets will be classified as either held-to-maturity, held-for-trading or available-for-sale. Held-to-maturity classification will be restricted to fixed maturity instruments that the company intends and is able to hold to maturity and will be accounted for at amortized cost. Held-for-trading instruments

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

will be recorded at fair value with realized and unrealized gains and losses reported in net income. The remaining financial assets will be classified as available-for-sale. These will be recorded at fair value with unrealized gains and losses reported in a new category of the consolidated balance sheet under shareholders' equity called other comprehensive income ("OCI"); and

- Derivatives will be classified as held-for-trading unless designated as hedging instruments. All derivatives, including embedded derivatives that must be separately accounted for, will be recorded at fair value on the consolidated balance sheet. For derivatives that hedge the changes in fair value of an asset or liability, changes in the derivatives' fair value will be reported in net income and be substantially offset by changes in the fair value of the hedged asset or liability attributable to the risk being hedged. For derivatives that hedge variability in cash flows, the effective portion of the changes in the derivatives' fair value will be initially recognized in OCI and the ineffective portion will be recorded in net income. The amounts temporarily recorded in OCI will subsequently be reclassified to net income in the periods when net income is affected by the variability in the cash flows of the hedged item.

The above guidance will apply for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2006. Earlier adoption will be permitted only as of the beginning of a fiscal year. The impact of implementing these new standards is not yet determinable as it is highly dependent on fair values, outstanding positions and hedging strategies at the time of adoption.

In October 2005, the Emerging Issues Committee of the CICA (the "EIC") issued Abstract No. 157, "Implicit Variable Interests Under AcG-15" (EIC-157), to address whether a company has an implicit variable interest in a VIE or potential VIE when specific conditions exist. An implicit variable interest acts the same as an explicit variable interest except it involves the absorbing and/or receiving of variability indirectly from the entity (rather than directly). The identification of an implicit variable interest is a matter of judgment that depends on the relevant facts and circumstances. EIC-157 will be effective in the first quarter of 2006. The implementation of this EIC is not expected to have a material impact on the company's consolidated financial statements.

In June 2005, the AcSB issued Handbook Section 3831, *Non-Monetary Transactions*, replacing Section 3830 of the same title. The new accounting standard requires all non-monetary transactions be measured at fair value unless certain conditions are satisfied. The new requirements are effective for non-monetary transactions initiated in periods beginning on or after January 1, 2006. The Company is in the process of evaluating the impact of the recently issued standard, but does not expect that the new standard will have a material impact on its financial position or results of operations.

### U.S. Pronouncements

In December 2004, the Financial Accounting Standards Board ("FASB") issued SFAS No. 123(R), *Share-Based Payment*, which establishes accounting standards for all transactions in which an entity exchanges its equity instruments for goods and services. SFAS No. 123(R) focuses primarily on accounting for transactions with employees. SFAS No. 123(R) eliminates the intrinsic value measurement objective in APB Opinion 25 and generally requires the Company to measure the cost of employee services received in exchange for an award of equity instruments based on the fair value of the award on the date of the grant. The standard requires grant date fair value to be estimated using either an option-pricing model which is consistent with the terms of the award or a market observed price, if such a price exists. Such cost must be recognized over the period during which an employee is required to provide service in exchange for the award in the requisite service period (which is usually the vesting period). The standard

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

also requires the Company to estimate the number of instruments that will ultimately be issued, rather than accounting for forfeitures as they occur.

The Company is required to apply SFAS No. 123(R) beginning with its fiscal year beginning January 1, 2006. SFAS 123(R) allows for either the "modified prospective method" or the "modified retrospective method" of recognizing compensation expense. Under the modified retrospective method, the Company must restate its previously issued financial statements to recognize the amounts the Company previously calculated and reported on a pro forma basis, as if the prior standard had been adopted. Under both methods, the Company is permitted to use either a straight line or an accelerated method to amortize the costs as an expense for awards with graded vesting.

The Company currently intends to adopt SFAS No. 123(R) using the modified prospective method. The Company expects that the adoption of SFAS No. 123(R) will result in an increase to operating expenses under U.S. GAAP in 2006 of approximately \$565.

In November 2004, the FASB issued SFAS No. 151, Inventory Costs an amendment of ARB No. 43, Chapter 4, which amends Chapter 4 of ARB No. 43 that deals with inventory pricing. The Statement clarifies the accounting for abnormal amounts of idle facility expenses, freight, handling costs, and spoilage. Under previous guidance, paragraph 5 of ARB No. 43, chapter 4, items such as idle facility expense, excessive spoilage, double freight, and rehandling costs might be considered to be so abnormal, under certain circumstances, as to require treatment as current period charges. This Statement eliminates the criterion of "so abnormal" and requires that those items be recognized as current period charges. Also, this Statement requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. This Statement is effective for inventory costs incurred during fiscal years beginning after June 15, 2005, although earlier application is permitted for fiscal years beginning after the date of issuance of this Statement. Retroactive application is not permitted. Management is analyzing the requirements of this new Statement and believes that its adoption will not have any significant impact on the Company's financial position, results of operations or cash flows.

In December 2004, the FASB issued SFAS No. 153, Exchanges of Nonmonetary Assets an amendment of APB No. 29. This Statement amends Opinion 29 to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. The Statement specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. This Statement is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in fiscal periods beginning after the date this Statement is issued. Retroactive application is not permitted. The Company is analyzing the requirements of this new Statement and believes that its adoption will not have any significant impact on the Company's financial position, results of operations or cash flows.

In November 2005, the FASB issued FSP FAS 115-1 and FAS 124-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments", which nullified 2004 guidance issued by the EITF on determining whether an impairment is other-than-temporary, and effectively reverted back to previous guidance in this area. The FSP generally encompasses guidance for determining when an investment is impaired, how to measure the impairment loss, and what disclosures should be made regarding impaired securities. This FSP is effective for the first quarter of 2006 is not expected to have a material impact on the Company's consolidated financial statements.

In June 2004, the FASB issued an exposure draft of a proposed Statement, "Fair Value Measurements" to provide guidance on how to measure the fair value of financial and non-financial assets and liabilities

## Notes to consolidated financial statements (continued)

(in thousands of Canadian dollars, except per share data and unless otherwise stated)

when required by other authoritative accounting pronouncements. The proposed statement attempts to address concerns about the ability to develop reliable estimates of fair value and inconsistencies in fair value guidance provided by current U.S. GAAP, by creating a framework that clarifies the fair value objective and its application in GAAP. In addition, the proposal expands disclosures required about the use of fair value to remeasure assets and liabilities. The standard will be effective for fiscal years beginning after December 15, 2006, and interim periods in those fiscal years, except that the disclosure requirements will be effective for fiscal years ending after December 15, 2006.

In May 2005, the FASB issued SFAS No. 154, "Accounting Changes and Error Corrections", which requires that changes in accounting principle be retrospectively applied as of the beginning of the first period presented as if that principle had always been used, with the cumulative effect reflected in the carrying value of assets and liabilities as of the first period presented and the offsetting adjustments recorded to opening retained earnings. SFAS No. 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005 with early adoption permitted. The Company is reviewing the guidance to determine the potential impact, if any, on its consolidated financial statements.

In June 2005, the FASB published an Exposure Draft containing proposals to change the accounting for business combinations. The proposed standards would replace the existing requirements of the FASB's Statement No. 141, *Business Combinations*. The proposals would result in fewer exceptions to the principle of measuring assets acquired and liabilities assumed in a business combination at fair value. Additionally, the proposals would result in payments to third parties for consulting, legal, audit, and similar services associated with an acquisition being recognized generally as expenses when incurred rather than capitalized as part of the business combination. The FASB also published an Exposure Draft that proposes, among other changes, that noncontrolling interests be classified as equity within the consolidated financial statements. The FASB's proposed standard would replace Accounting Research Bulletin No. 51, *Consolidated Financial Statements*.

On July 14, 2005, the FASB published an exposure draft entitled *Accounting for Uncertain Tax Positions* — an interpretation of FASB Statement No. 109. The proposed interpretation is intended to reduce the significant diversity in practice associated with recognition and measurement of income taxes by establishing consistent criteria for evaluating uncertain tax positions. The proposed interpretation would be effective for the first fiscal year beginning after December 15, 2006. Earlier application would be encouraged. Only tax positions meeting the probable recognition threshold at that date would be recognized. The transition adjustment resulting from application of this interpretation would be recorded as a cumulative-effect change in the income statement as of the end of the period of adoption. Restatement of prior periods or pro forma disclosures under APB Opinion No. 20, *Accounting Changes*, would not be permitted. Management is in the process of reviewing the requirements of this recent exposure draft.

On September 30, 2005, the FASB issued an Exposure Draft that would amend FASB Statement 128, *Earnings per Share*, to clarify guidance for mandatorily convertible instruments, the treasury stock method, contracts that may be settled in cash or shares and contingently issuable shares. The proposed Statement would be effective for interim and annual periods ending after June 15, 2006. Retrospective application would be required for all changes to Statement 128, except that retrospective application would be prohibited for contracts that were either settled in cash prior to adoption or modified prior to adoption to require cash settlement. Management is in the process of reviewing the requirements of this recent exposure draft.

## REPORT OF INDEPENDENT REGISTERED CHARTERED ACCOUNTANTS

To the Board of Directors and Shareholders of NovAtel Inc.,

We have audited the consolidated financial statements of NovAtel Inc. as at December 31, 2005 and 2004, and for each of the years in the three year period ended December 31, 2005, and have issued our reports thereon dated February 9, 2006 (which audit report expresses an unqualified opinion and includes an explanatory paragraph referring to our consideration of internal control over financial reporting and also includes a separate report titled Comments by Independent Registered Chartered Accountants for U.S. Readers on Canada — U.S. Reporting Differences referring to changes in accounting principles that have a material effect on the comparability of the Company's financial statements and changes in accounting principles that have been implemented in the Company's financial statements); such financial statements and reports are included in the 2005 Annual Report on Form 20-F. Our audits also included the financial statement schedule of NovAtel Inc. This financial statement schedule is the responsibility of the Company's management. Our responsibility is to express an opinion based on our audits. In our opinion, the financial statement schedule, when considered in relation to the basic financial statements taken as a whole, present fairly, in all material respects, the information set forth therein.

(signed) "Deloitte & Touche LLP"

Deloitte & Touche LLP  
Independent Registered Chartered Accountants  
Calgary, Alberta, Canada  
February 9, 2006

**SCHEDULE II**  
**Valuation and Qualifying Accounts**  
**(in thousands, Canadian dollars)**

<u>2003</u>	<u>Balance at beginning of period</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance at end of period</u>
Allowance for doubtful accounts and provision for sales returns .....	\$1,077	430	(429)	\$1,078
Provision for future warranty costs .....	\$ 344	220	(154)	\$ 410
 <u>2004</u>	 <u>Balance at beginning of period</u>	 <u>Additions</u>	 <u>Deductions</u>	 <u>Balance at end of period</u>
Allowance for doubtful accounts and provision for sales returns .....	\$1,078	215	(86)	\$1,207
Provision for future warranty costs .....	\$ 410	312	(184)	\$ 538
 <u>2005</u>	 <u>Balance at beginning of period</u>	 <u>Additions</u>	 <u>Deductions</u>	 <u>Balance at end of period</u>
Allowance for doubtful accounts and provision for sales returns .....	\$1,207	29	(156)	\$1,080
Provision for future warranty costs .....	\$ 538	382	(227)	\$ 693

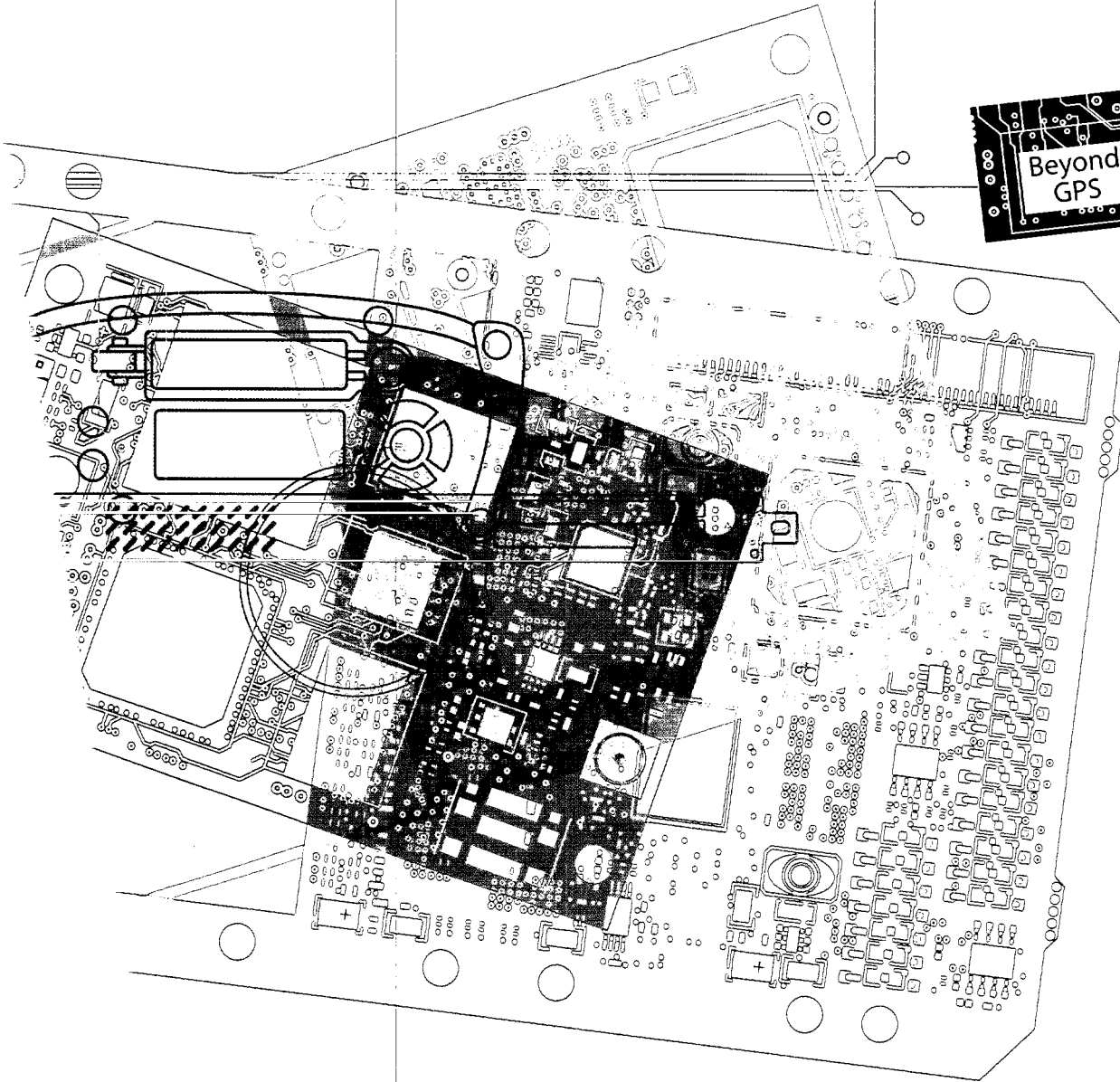
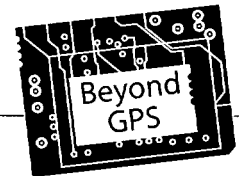


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precise thinking

2005 Annual Report



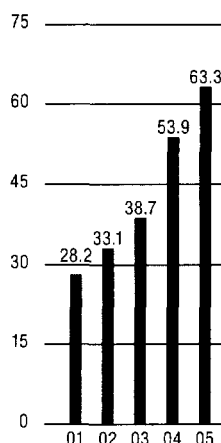
NovAtel Inc. designs, markets and sells high-precision GPS and other positioning components and sub-systems. We supply our core technology to original equipment manufacturers (OEMs) and system integrators who build systems for various commercial end market applications, principally in the geomatics (surveying and mapping), aviation, mining, precision agriculture, marine and defence industries. NovAtel is also the principal supplier of reference receivers to national aviation ground networks in the US, Japan, Europe, China and India. Our solutions combine hardware, such as receivers and antennas, with software to enable our customers to fully integrate NovAtel's high-precision GPS technology into their respective products and systems. For more up-to-date information, visit [www.novatel.com](http://www.novatel.com).

## 2005 Highlights

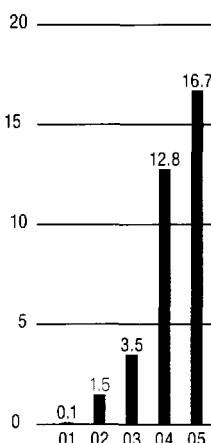
### 2005 Overall Results

2005 was the most successful year in NovAtel's history as we executed our strategies and achieved strong revenue and profitability growth. We achieved year-over-year revenue growth of 17% to a record C\$63.3 million, despite a significant negative impact due to foreign exchange, and we achieved net income growth of 30% to a record C\$16.7 million. We believe our strong financial performance in 2005 continues to be a result of our approach of building strong relationships and market share with large OEM customers and emerging system integrators. We achieved strong financial results in 2005 while at the same time investing 17% of revenue in research and development on innovative "GPS-Plus" technologies.

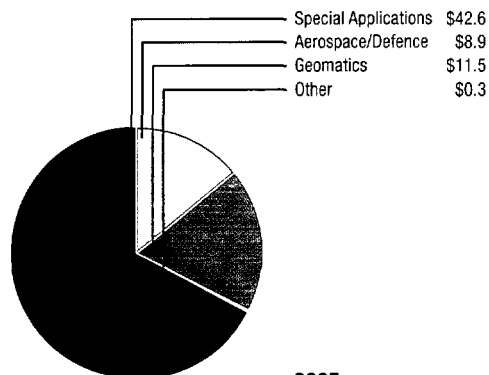
**Revenues**  
CDN\$ millions



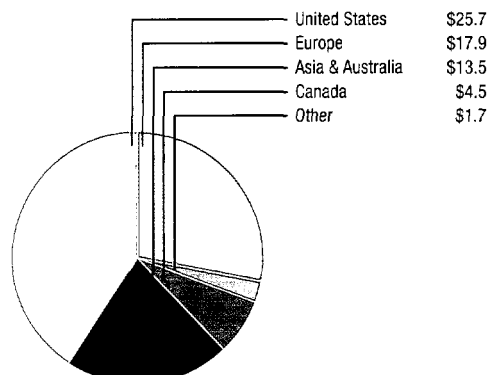
**Net Income**  
CDN\$ millions

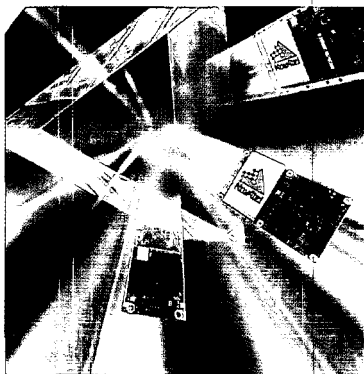


**2005 Sales by Category**  
CDN\$ millions



**2005 Sales by Geography**  
CDN\$ millions





## New Technology

In 2005 we announced OEMV, our next generation of receiver engines. At the heart of the OEMV technology is a new digital chip that represents an order of magnitude advancement in technology and feature integration over our previous high-performance receivers. The OEMV family of products is also fully RoHS (Restriction of Hazardous Substances) compliant, meeting the European Economic Union's directive to reduce the hazardous materials content in electronic products. The OEMV-2 and OEMV-3 models are drop-in replacements for our existing OEM-4 components, and include dual-frequency GLONASS measurements as an option. GLONASS is a satellite positioning system established by the former Soviet Union and operated by the Russian government. GPS, GLONASS and the European Union's future Galileo are collectively known as the Global Navigation Satellite System, or GNSS. Providing our customers with the option of highly integrated GPS+GLONASS is an excellent example

of how our development teams drive technical innovation and integration to create compelling price/performance and return on investment for our customers worldwide. NovAtel also introduced its first dual-mode GPS+Galileo receiver in 2005.



## Special Applications

Revenue from NovAtel's Special Applications category contributed C\$42.6 million in 2005 and grew 29% compared to 2004. Key elements of this growth were shipments into China, the United States and Europe. Our business in China grew in 2005 compared to 2004, primarily driven by the developing OEM integration market in China, which is addressing domestic surveying and mapping applications, as well as emerging markets such as

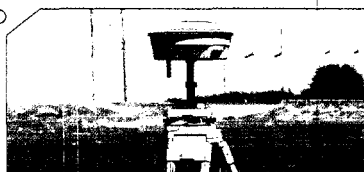
precision container tracking and placement. We experienced 35% growth in the United States across a number of vertical markets. Shipments into Europe also grew approximately 30%, primarily in the surveying and mapping market, and were largely driven by our strategic relationship with Leica Geosystems.



## Aerospace and Defence

NovAtel's Aerospace and Defence revenue decreased by 21% in 2005 compared to 2004. Our Aerospace and Defence revenue is highly variable due to its dependence on the timing of government contracts. The decrease in 2005 compared to 2004 was largely due to significant revenue received during 2004 related to three contracts with Raytheon Company for next-generation Wide Area Augmentation System (WAAS) programs. Late in 2005,

we began recognizing revenue from the first stages of a new contract we announced in December 2005 to develop the Ground Reference Receiver for Europe's future Galileo satellite navigation system.



## Geomatics

Revenue from NovAtel's Geomatics category in 2005 grew 24% compared to 2004, primarily due to new customers and partially due to higher revenue associated with Point, Inc., our joint venture with Sokkia Co., Ltd. of Japan. During 2005, we achieved significant revenue increases with Geomatics-related customers in Asia and Canada. We also view the revenue trend at Point as an indication that our mutual efforts with Point and Sokkia, to improve the

operating performance at Point, is working. During the fourth quarter 2005, Sokkia launched their next-generation, dual-frequency surveying system. This newly developed Point product, the GSR2700IS, has NovAtel's advanced receiver and antenna technology onboard and incorporates a number of innovative and competitive user features.

## Acquisition



During the fourth quarter of 2005, we announced the acquisition of Waypoint Consulting Inc., a Calgary-based, precise positioning software company that produces

real-time and post-processing position determination software using input from precision GPS and GPS/inertial systems. Waypoint's software is very complementary to our technology, and addresses growing customer demand for specialized GPS and GPS/inertial positioning and trajectory software and systems.

# To our shareholders

2005 marked a fifth consecutive year of profitable growth for NovAtel Inc. as our revenue and net income reached new historical levels. Since 2002, revenue has grown at a compound annual growth rate of 24% and operating income has grown at a compound annual growth rate of approximately 77%. Our focus is on our growing global base of commercial customers as we execute our "NovAtel Onboard™" strategy—providing a growing number of precise positioning components and subsystems that offer compelling competitive price performance. Our customers rely on our commitment to technology leadership in precise positioning technology, and in 2005 we invested 17% of revenue into research and development. As well, we launched our next generation of highly integrated precise positioning components, the OEMV family of receivers. These receivers can simultaneously track GPS as well as the Russian GLONASS satellites. This dual-constellation capability will provide customers with more availability of precise positioning, even in partially obstructed environments where GPS-only systems are challenged. We are pleased to report that, even given the large expenditures on R&D in 2005, we continued to drive greater operating efficiency and return on investment (ROI), and increased our operating margins to a robust 22% of revenue.

Revenues for 2005 compared to 2004 grew 17% to C\$63.3 million and net income for the same period grew 30% to C\$16.7 million, or C\$1.91 per share (diluted). This growth was achieved despite the impact of the weaker US dollar, which decreased in value relative to the Canadian dollar in 2005. In US dollars, which is the base currency of the majority of our revenue, our sales in 2005 grew at a rate of approximately 25% compared to 2004.

2005 set the stage for future growth with the introduction of our next generation technology, the OEMV family of receivers

The profitable growth we have experienced over the past five years has resulted in 17 consecutive quarters of positive cash flow and a strong balance sheet. We ended 2005 with cash and short term investments of C\$35.1 million, which is vital to our strategy of growing the company inorganically through acquisitions. In the fourth quarter of 2005 we acquired Waypoint Consulting Inc. Waypoint's software products are a key component of our "GPS+" strategy, especially in our SPAN product line where we are integrating GPS and inertial systems. Waypoint's talented employees have been a welcome addition to our existing highly skilled NovAtel team.

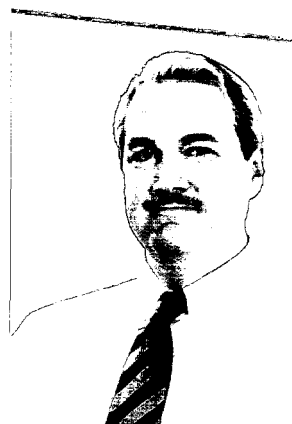
## Growing OEM business

Our growth continues to be driven by our largest revenue category, Special Applications, which grew 29% in 2005 compared to 2004 and contributed C\$42.6 million to revenue. Special Applications forms the core of our business and is made up primarily of sales to large OEMs and system integrators who incorporate our technology into their end-user solutions. A significant growth driver in Special

Applications is our business into China, which grew 62% in 2005 compared to 2004. China has a developing OEM integration market that is addressing domestic surveying, mapping, port automation and other applications that require precise positioning and navigation.

We also achieved approximately 35% growth in the United States across a number of vertical markets, as well as increased shipments to Europe. Our sales into Europe are primarily for the surveying and mapping market through our strategic relationship with Leica Geosystems AG, which is our largest customer and comprised 18% of our total revenue in 2005. This successful relationship continues to be an excellent example of our "NovAtel Onboard" strategy, as we work closely with Leica to develop technology and components in support of their future product roadmaps. NovAtel technology is currently onboard a growing number of Leica's surveying, reference station and machine control products, including their recently announced GPS 1200 products. We expect growth in mature markets, such as geomatics, to accelerate as demand grows for our new receivers and antennas that now support multi-constellation signals.

We also expect continued long-term growth in Special Applications from a number of other vertical markets, including precision agriculture. AGCO, a multi-billion dollar agricultural corporation, announced in 2005 that it has assumed responsibility for the assembly and distribution



**Jonathan W. Ladd**  
President and  
Chief Executive Officer

of its NovAtel GPS-based steering systems, sold under AGCO's Auto-Guide brand and as an aftermarket product under BEELINE Technologies, Inc.'s Arro brand. AGCO also announced that the availability of Auto-Guide has grown from a factory-installed option on one product line, the Challenger tractor, to multiple product lines and brands, including certain AGCO, Ag-Chem and Massey-Ferguson tractors, sprayers and applicators. We are working closely with AGCO on future products to support their global, precision agriculture roadmaps.

### **New generation of technology**

2005 set the stage for future growth with the introduction of our next generation technology, the OEMV family of single-frequency, dual-frequency and, for the first time, triple-frequency receivers. These products began rolling out on schedule in March of 2006. We have made a significant investment over the past few years to develop these products, and we are pleased that some of our largest customers have already released products with OEMV technology onboard.

For existing customers, the OEMV-2 and OEMV-3 models are drop-in replacements of our successful OEM4 receivers, making transition virtually effortless. OEMV technology sets a new standard in feature integration, multipath mitigation and price performance. OEMV technology includes the capability to precisely track the next-generation "modernized" GPS signals including the third L5 frequency, as well as dual-frequency signals from the growing Russian GLONASS satellite constellation. GLONASS is a satellite navigation system operated by Russia, and is complementary to the United States' GPS and the European Union's future Galileo systems. All three systems are referred to as the Global Navigation Satellite System, or GNSS. We were also the first to announce a single-board, dual-frequency GPS+Galileo receiver earlier this year. What does access to these myriad combinations of satellite signals and frequencies mean to our customers? Simply stated, the more satellites and frequencies simultaneously tracked, the more available and reliable the positioning and navigation solution, especially in partially obstructed environments. We believe that the new expanded GNSS capability on our core family of precision components will continue to create a compelling price performance ratio with superior return for our customers.

### **Galileo—a strategic win**

Late in 2005, we announced that we had been selected as a key technology contributor to the development team responsible for the ground-based segment of Galileo, Europe's future state-of-the-art satellite navigation system. This multi-year contract has the potential to generate up to €6.3 million of funded research and development by 2008. We are currently working on this program and have begun to realize revenue. We are very excited about our involvement in this program—not only are we working on critical elements of Galileo, but we believe our early funded development will drive competitive advantage in our future development of commercial Galileo products. The European Space Agency expects that Galileo will be operational in the 2008–2011 time frame.

Revenue from the Galileo program is recorded under our Aerospace and Defence business category that, as expected, experienced a decrease in 2005 compared to 2004. This decrease is not related to a loss of market share, rather, it is a consequence of the timing of certain programs and projects. For example, in 2004 we recorded significant revenue from the shipment of products to upgrade the US Wide Area Augmentation System (WAAS) civil navigation program. Such programs have defined start and end dates, vary in scope and do not necessarily occur on an annual basis. However, the long-term opportunities for regional satellite-based augmentation systems (SBAS) such as WAAS look promising. During 2005, we delivered receivers to Raytheon for initial testing of India's SBAS program, GAGAN, and we believe there is potential over the next few years as India and other countries decide to invest in the benefits of implementing SBAS programs.

The performance of our third business category, Geomatics, improved in 2005 compared to 2004, with revenue increasing 24% to C\$11.5 million. The majority of this increase was due to component sales to new customers in Canada and Asia, as well as increased revenue attributable to Point, Inc., our joint venture with Sokkia Co., Ltd. of Japan. Shipments began in late 2005 of a next-generation, dual-frequency surveying system, which Sokkia launched in late 2005. This system was jointly developed by Point and NovAtel and contains our advanced receiver and antenna technology onboard, as well as a number of innovative and competitive user features.



**Werner Gartner**  
Executive Vice President  
and Chief Financial Officer



**Patrick C. Fenton**  
Vice President and  
Chief Technology Officer

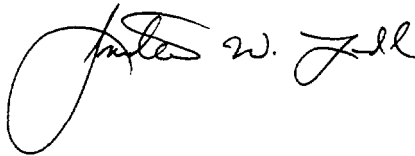
### Investment in our foundation

The steady growth we have achieved over the past five years has allowed NovAtel to add to its existing foundation of great, talented people. In 2005, we expanded in all areas—sales, marketing, administration, manufacturing, research and development—in order to remain positioned to deliver price-competitive products and technology. The number of full-time employees at NovAtel increased 20% in 2005 compared to 2004, and we opened a new office in Europe to expand our dealer network and to provide regional sales support. We welcome these new members to the NovAtel team as we work together to meet 2006 objectives. We also broke ground on an addition to our existing facility here in Calgary, Alberta and plan to begin occupying it in late summer 2006.

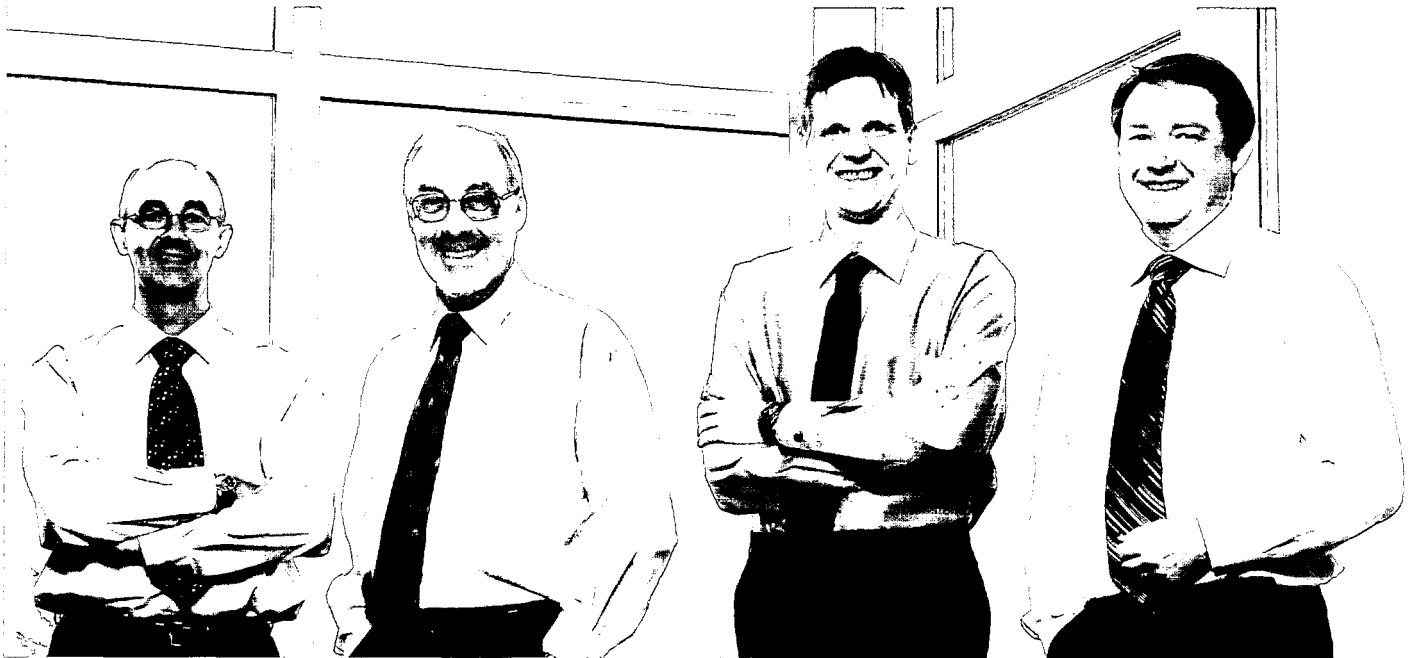
When a company experiences healthy growth, it is critical to remain mindful of operational efficiencies. In 2005, we continued to implement Lean Enterprise—a corporate culture of continuous improvement with the goals of improving quality, eliminating waste, reducing lead time and reducing total costs. We have implemented process improvements during the year in many areas—from improving our New Product Introduction Process, to major supply chain initiatives to drive shorter lead times and increased responsiveness to customer demand.

Looking forward, we plan to continue to execute our strategy of investing in technology leadership, improving processes, growing business with our current customers and working hard to gain new customers to drive future organic growth. We are also actively working to grow our company beyond organic means by deploying our growing cash position. We are looking for more partnership and acquisition opportunities that will provide access to complementary technologies to broaden our technology base, as well as opportunities that will allow us to access new customers and markets.

In closing, I must thank our customers, partners, employees and shareholders for making 2005 another exciting year for NovAtel Inc. Looking to the future, we believe that NovAtel is well positioned to take advantage of the positive growth dynamics that will result from the growing number of global satellite and augmentation systems. We look forward to continuing to report on our progress.



Jonathan W. Ladd  
President and Chief Executive Officer  
May 2006



**Mike McAloney**  
Vice President, Operations  
& Corporate Quality

**Tony Murfin**  
Vice President,  
Business Development

**Curtis Anderson**  
Vice President,  
OEM Product Development

**Graham Purves**  
Vice President, Sales

Not pictured: **Farlin Halsey**  
Vice President, Marketing

# Corporate Governance

## Directors

(as at May 18, 2006)

David E. Vaughn\*  
Chairman of the Board  
(President, Foursome Technologies)

Robert J. Iverach\*  
Director

Richard D. Orman\*\*  
Director  
(Chief Executive, Nor Energy AS)

Joel A. Schleicher\*  
Director  
(Chairman and Chief Executive Officer,  
Integrated Solutions, Inc.)

Charles R. Trimble\*  
Director  
(Chairman, United States  
GPS Industry Council)

Jonathan W. Ladd  
Director  
(President and Chief Executive Officer,  
NovAtel Inc.)

Werner Gartner  
Director  
(Executive Vice President and  
Chief Financial Officer,  
NovAtel Inc.)

Patrick C. Fenton  
Director  
(Vice President and  
Chief Technology Officer, NovAtel Inc.)

\* Audit Committee \*\* Compensation Committee

## Executive Officers and Key Employees

Jonathan W. Ladd  
President, Chief Executive Officer

Werner Gartner  
Executive Vice President,  
Chief Financial Officer

Patrick C. Fenton  
Vice President, Chief Technology Officer

Curtis Anderson  
Vice President, OEM Product Development

Farlin A. Halsey  
Vice President, Marketing

Michael McAloney  
Vice President,  
Operations and Corporate Quality

Anthony J. Murfin  
Vice President, Business Development

Graham C. Purves  
Vice President, Sales

## Committees of the Board of Directors

### Audit Committee

The Audit Committee assists NovAtel's Board of Directors in fulfilling its responsibilities for oversight and supervision of financial and accounting matters. The Audit Committee's responsibilities include: engaging or discharging the independent auditors; reviewing, with the independent auditors, the plan and results of the auditing engagement; reviewing NovAtel's internal auditing procedures, system of internal accounting controls and financial management; and making inquiries into matters within the scope of this Committee's functions. The Board of Directors and the Audit Committee have adopted a written charter of the Audit Committee, which may be viewed on NovAtel's website, [www.novatel.com](http://www.novatel.com).

### Compensation Committee

The function of the Compensation Committee is to ensure that NovAtel has a high caliber of executive management in place and a total compensation plan that is competitive, motivating and rewarding for participants. The Compensation Committee reviews and makes recommendations to the NovAtel Board of Directors concerning the compensation of the key management employees of the Company and the administration of the compensation plans.

## NovAtel Corporate Policies

### Code of Ethics and Business Conduct

NovAtel Inc. is determined to conduct its business in strict compliance with all applicable laws, rules and regulations; with honesty and integrity; and with a strong commitment to the highest standards of ethics and business conduct. The Company's employees are expected to conduct business affairs within both the letter and the spirit of the law. A basic principle is that integrity must guide the Company in all dealings with all parties. The entire policy may be viewed on NovAtel's website, [www.novatel.com](http://www.novatel.com).

### Insider Trading Policy

All employees, directors, officers and affiliates are required to comply with NovAtel's Insider Trading Policy. The entire policy may be viewed on NovAtel's website, [www.novatel.com](http://www.novatel.com).

NOVATEL is a trademark of NovAtel Inc., is Registered in the U.S. Patent and Trademark Office and in Canada, and the NOVATEL mark is the subject of registrations and pending applications to register the mark elsewhere internationally. NOVATEL ONBOARD and VISION CORRELATOR are trademarks of NovAtel Inc., are Registered in Australia, and are the subject of pending applications to register each mark in the U.S., Canada and elsewhere internationally.

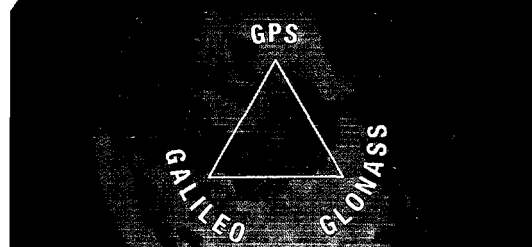


# Generating Growth

NovAtel's mission is to be the leading provider of precise global positioning plus augmentation technologies that afford our customers rapid integration and exceptional return on investment. It is crucial that our technology and product solutions meet the evolving requirements of our customers worldwide—when our customers succeed, we succeed.

NovAtel's highly skilled team of over 200 employees is dedicated to ensuring that we meet the current and future needs of over 400 customers around the world. Attracting and retaining the best performance-motivated employees is an important aspect of NovAtel's success.

## GLOBAL NAVIGATION SATELLITE SYSTEM



## Investing in high-precision positioning technology

NovAtel's research focuses on growth through core innovation and integration—the integration of GPS with other satellite systems, as well as the combination of our technology with other complementary technologies.

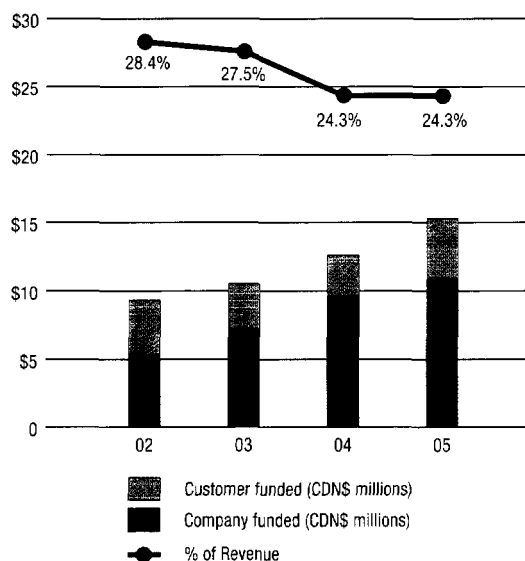
In 2005, we integrated an innovative new technology—Vision Correlator™. This technology uses a new patented approach in hardware and software that virtually eliminates errors caused by multipath, where reflected signals interfere with the direct line-of-sight satellite signals. By further improving signal tracking integrity, NovAtel continues to offer the highest levels of satellite signal measurement fidelity which equates to improved reliability and accuracy for our customers.

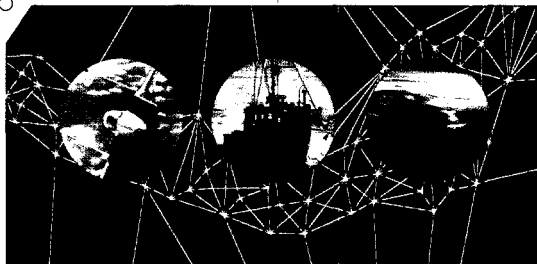
In 2005, we developed OEMV, our next generation of single-frequency, dual-frequency and now, triple-frequency receiver engines. The OEMV family is the result of many years and millions of dollars spent to develop innovative core technology that is also capable of using signals from GPS and Russian GLONASS. Currently, both the US Government's GPS satellites and the Russian Government's GLONASS satellites orbit the Earth; within the next few years, they will be joined by Galileo satellites launched by the European Union. Together, these constellations are known as the Global Navigation Satellite System (GNSS).

With GNSS, a new era begins in satellite navigation. The opportunity exists for more mature markets, such as geomatics, to grow at higher than expected rates due to the true and measurable benefit a customer can achieve using multi-constellation receivers. Our customers will benefit from products that are designed to use the signals from these multiple systems—the more satellites a receiver can track at the same time, the more available and reliable the positioning and navigation solution. Having better access to precise positioning, even in obstructed environments where GPS alone doesn't work, will drive faster return on investment by expanding the utilization of our customers' products.

## R&D Expenditures

A key element of NovAtel's growth strategy is continued substantial investment in research and development, while maintaining operating income margins to ensure continued profitability.





## Acquiring technology

A significant element of our growth strategy is to gain access to technologies that will broaden our current product offering. NovAtel is continually seeking to develop strategic partnerships with industry leaders of enabling and complementary technologies, such as inertial systems, guidance technology and wireless communications. We are also pursuing selective strategic acquisitions that are complementary to current product offerings to expand our market opportunity or broaden our technology offering.

Our acquisition of Waypoint Consulting Inc. in 2005 is an excellent example of this aspect of our growth strategy. The acquisition immediately broadened our base of core precise positioning technology and enabled us to address growing customer demand for specialized real-time and post-processing GPS and GPS/inertial positioning and trajectory software. We have also begun integrating Waypoint's technology into our successful SPAN Technology™, which combines GPS with an inertial measurement unit to meet customer demand for precise position, velocity, time and attitude data in challenging environments where satellites can become obstructed. The initial market demand for SPAN Technology has exceeded our expectations, and the integration of Waypoint's technology is expected to make SPAN an even stronger product offering for NovAtel.



## Galileo—Europe's answer to GPS

Galileo will be Europe's own global navigation satellite system, and the European Space Agency has announced they expect it to be operational in the 2008 to 2011 time frame. It will be interoperable with GPS and GLONASS, the two other global navigation satellite systems. The Galileo initiative was launched by the European Union and the European Space Agency, and is designed as a non-military system supporting both civilian and government purposes.

NovAtel has been involved in Galileo programs since 2000, including feasibility studies, concept demonstrations, development of a dual GPS/Galileo test receiver, and initial development of the Galileo system ground reference receiver. Our early involvement, which was funded through contracts received from the Canadian Space Agency, has allowed us to develop core Galileo technology well in advance of the deployment of the operational system.

We have now incorporated these earlier development efforts into a new program to develop, qualify and supply receiver components—key elements of the Galileo system's ground infrastructure. The initial funding of €1.3 million was announced in late 2005, and if our involvement continues, the fully funded program could be worth €6.3 million between now and 2008.

Earlier this year, we announced the availability of our first GPS+Galileo receiver and antenna. Over the long term, we expect that growth in sales of commercial receivers will be driven by customer demand for the benefits that multiple global navigation satellite systems can provide. We anticipate that when Galileo becomes operational, GPS and Galileo, as well as GLONASS, will be used together to significantly improve the quality and reliability of satellite navigation.

## Market Information

NovAtel Inc.'s common shares have been listed on The Nasdaq Stock Market® since February 7, 1997. The following are the price ranges as reported by The Nasdaq Stock Market® for the periods indicated.

(US\$)	High	Low
<b>Year Ended December 31, 2005</b>		
First Quarter	48.450	16.260
Second Quarter	29.190	14.318
Third Quarter	37.150	22.190
Fourth Quarter	31.760	21.690
<b>Year Ended December 31, 2004</b>		
First Quarter	18.900	8.070
Second Quarter	15.470	9.500
Third Quarter	14.990	8.540
Fourth Quarter	50.350	11.390
<b>Year Ended December 31, 2003</b>		
First Quarter	3.500	1.900
Second Quarter	4.190	2.840
Third Quarter	4.980	3.250
Fourth Quarter	11.080	4.660
<b>Year Ended December 31, 2002</b>		
First Quarter	4.000	2.100
Second Quarter	5.200	2.550
Third Quarter	2.840	1.810
Fourth Quarter	2.820	1.760
<b>Year Ended December 31, 2001</b>		
First Quarter	2.688	1.281
Second Quarter	2.100	1.250
Third Quarter	2.310	1.300
Fourth Quarter	3.050	1.400

The Company has not declared or paid any dividends on the common shares to date. The payment of dividends in the future will be dependent on the earnings and financial condition of the Company and on such other factors as the NovAtel Board of Directors considers appropriate.

## Forward-looking Statement

Certain statements in this annual report, including those about the Company's future plans and intentions, financial guidance, long-term growth prospects, levels of activity or other future events, are forward-looking statements for purposes of the Safe Harbor Provisions under the SEC's Private Securities Litigation Reform Act of 1995. These forward-looking statements are not based on historical facts, but rather on management's current expectations regarding NovAtel's future growth, results of operations, performance, future capital and other expenditures, competitive advantages, business prospects and opportunities. Forward-looking statements involve significant known and unknown risks, uncertainties and assumptions. Many factors could cause actual results, performance or achievements to differ materially from the results discussed or implied in the forward-looking statements, including impact and timing of large orders, U.S. dollar to Canadian dollar exchange rate fluctuations, and other factors described in the Company's Form 20-F and other SEC filings. These factors should be considered carefully and undue reliance should not be placed on the forward-looking statements. These forward-looking statements are made as of the date of this Annual Report, and NovAtel assumes no obligation to update or revise them to reflect new events or circumstances.

## Shareholder Information

### Headquarters

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1120 – 68th Avenue NE  
Calgary, Alberta, Canada  
T2E 8S5

Telephone: (403) 295-4500  
Fax: (403) 295-0230

Investor Relations  
and requests for 20-F:  
(403) 295-4532, ir@novatel.ca

Website: www.novatel.com

### Stock Exchange Listing

Listed on The Nasdaq  
Stock Market®  
Stock Symbol: NGPS



### Annual Meeting

9:00 am MT  
July 18, 2006  
Sheraton Cavalier Hotel  
32 Avenue NE  
Calgary, Alberta, Canada

### Transfer Agent

Mellon Investor Services LLC  
Shareholder Relations

PO Box 3315  
South Hackensack, NJ, USA  
07606  
or

480 Washington Boulevard  
Jersey City, NJ, USA 07310-1900

Telephone:  
800-522-6645  
TDD for Hearing Impaired:  
800-231-5469  
Foreign Shareholders:  
(201) 680-6578  
TDD Foreign Shareholders:  
(201) 680-6610

Website:  
www.melloninvestor.com/isd

### Independent Auditors

Deloitte & Touche LLP  
Independent Registered  
Chartered Accountants  
Calgary, Alberta, Canada



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[ir@novatel.ca](mailto:ir@novatel.ca)

[sales@novatel.ca](mailto:sales@novatel.ca)

U.S. & Canada

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+1 403 295 4900